State Retirement
SRAC
Advisory Commission

# STATE RETIREMENT ADVISORY COMMISSION
# FINAL REPORT

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SRAC
Advisory Commission

Karen Winn, Chairperson

September 29, 2000

Mr. Jerry Conley, Chairman
Ad Hoc Task Force on Total Compensation
c/o Missouri Department of Conservation
P.O. Box 180
2901 W. Truman Blvd.
Jefferson City, MO 65102

Dear Jerry:

On behalf of the State Retirement Advisory Commission (SRAC), I am pleased to present our findings and recommendations pertaining to certain legislative proposals that were introduced last session, and other recommendations relating to retirement, to the Ad Hoc Task Force on Total Compensation (TFTC).

The SRAC recognized the importance of the charge given to them in the Governor's Executive Order and was mindful of seeking out fiscally responsible solutions that would ensure a fair and equitable benefit plan for all state employees.

It is our sincere hope that these recommendations, as well as the other information contained in this report, will be useful to the TFTC, the Governor and the General Assembly, in our collective efforts to provide state employees with financial security in an equitable and cost-effective manner.

Sincerely,

Karen a. Winn

Karen Winn
Chairperson, State Retirement
Advisory Commission

Enclosure

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# STATE RETIREMENT ADVISORY COMMISSION
# FINAL REPORT

## Executive Summary

Earlier this year, the Governor issued an executive order establishing the State Retirement Advisory Commission (SRAC). The role of the SRAC was to evaluate legislative proposals introduced during the second regular session of the 90th General Assembly that would have modified the structure of any benefits provided by the state retirement plans.

After meeting frequently in a compressed time frame and giving consideration to the issues related to relevant legislative proposals, the SRAC reached the following conclusions:

1) That valuable, long-service employees could possibly be induced to delay their retirement if a Deferred Retirement Lump Sum Option (DROP) was added to the current menu of retirement options, thus affording state agencies the opportunity to further enhance their succession planning efforts, and ease the transition problems associated with retirement. The SRAC recommends that legislation be drafted and introduced that would make the proposed back DROP model described on page 11 available to members retiring under Chapter 104, RSMo (other than elected officials and members of the general assembly).

2) That establishing an Optional Retirement Plan (ORP) for the regional colleges and universities would run counter to the "attract and retain" philosophy that has been promoted by the state and endorsed in the Year 2000 Plan. However, given the fact that considerable legislative support for an ORP exists in the General Assembly, the SRAC recommends the proposed university retirement plan (URP) described on pages 21-22 of this report. The URP approach would address most of the problematic design issues associated with past ORP proposals – specifically, those concerns that deal with equal protection, adverse selection, and irrevocable elections.

3) That the issues associated with offering separate benefits for public safety employees have been sufficiently and thoroughly explored by the Public Safety Retirement Advisory Commission (PSRAC), and resolved through the enactment of the Year 2000 Plan. The SRAC is supportive of the equity concept that suggests that the state should not differentiate in benefit levels for general employees and public safety like classifications. The SRAC voted not to support the additional one-third retirement benefit for conservation agents and special death and burial benefits for state public safety employees.

4) That the criteria for membership in the Administrative Law Judges' and Legal Advisors' Plan (ALJLAP) be carefully examined and clarified in order to avoid future litigation. Items for consideration might include term limits or recruitment late in an employee's career versus denominators that are common throughout state government. The SRAC also recommends that a separate commission be appointed to further evaluate the criteria for membership in the ALJLAP and to determine whether or not sufficient evidence exists to expand, limit or contract membership in the system in the future.

5) That providing the 1.7% formula in the closed plan would be a step backward in the pursuit of benefit equity. The Year 2000 Plan was designed to specifically achieve certain policy and personnel objectives, correct benefit inequities, promote individual choice (current retirees may elect to transfer to the Year 2000 Plan), and to accomplish all of these goals without increasing the state's costs for retirement programs. The SRAC noted that the 1.7% formula is already available to all past, present, and future employees through the new plan and to incorporate that formula in the old plan would create a benefit disparity between the new and old plans.

6) That given the current volatile nature of the health care industry, the SRAC believes a service-based health care model will serve as a future cost containment measure and will also ensure that the same quality of care is available to both the highest and lowest paid employees. The SRAC recommends adoption of a model that provides a subsidy towards a retiree's monthly premium of 2.5% per year of service based upon the applicable low cost plan option for each full year of actual state service with a maximum subsidy of 75%. In light of the increased subsidy to retiree health care that occurred after the SRAC completed its activity, the SRAC recommends that the Ad Hoc Task Force on Total Compensation (TFTC) work closely with the Missouri Consolidated Health Care Plan to further investigate the impact of the recent increased subsidy for retiree health care and how that increase might affect the recommended service-based model.

7) That the issue of pension tax exemption legislation extends beyond the scope of the charge of the SRAC and therefore should be evaluated by those with expertise in the taxation/revenue area.

8) That the SRAC is supportive of measures that provide better coordination of benefits and communications that work in the best interest of the plan participants. The SRAC recommends that the Deferred Compensation Commission and the Missouri State Employees' Retirement System continue to work towards achieving improved service delivery and a better understanding by state employees of the overall benefit package.

9) That upon the expiration of the TFTC's term, a similar board or commission be established through enabling legislation. This new board or commission would be given the task of evaluating policy and recommended courses of action relating to total compensation, retirement, health care, and other benefits for state employees under the Executive Branch on a permanent basis.

The TFTC is obligated to submit to the Governor, no later than November 30, 2000, a separate addendum to the final report which contains the TFTC's recommended course of action.

For reporting purposes, the SRAC has addressed the issues related to the individual legislative proposals introduced last session under the broad captions of a) Workforce Shortage; b) Reciprocity, Portability, and Public Employee Retirement Plans; c) Benefit Equity; and d) Financial Security in Retirement. An analysis of each legislative proposal can be found in the pages that follow.

# INTRODUCTION

## The State Retirement Advisory Commission

The State Retirement Advisory Commission (SRAC) was created under Executive Order 00-11 and is comprised of appointed members from the Ad Hoc Task Force on Total Compensation (TFTC); the Missouri State Employees' Retirement System (MOSERS); the Highway and Transportation Employees' and Highway Patrol Retirement System (HTEHPRS); the Missouri General Assembly's Joint Committee on Public Employee Retirement; and the Administrative Hearing Commission. The Commissioner of Administration; the Director of the Department of Public Safety; and the Commissioner of Higher Education were also appointed to serve on the SRAC.

The SRAC was created on the premise that a comprehensive approach to evaluating employee benefits was preferable to the fragmented fashion in which employee benefits have evolved over the years. The SRAC was charged with the task of evaluating legislative proposals introduced during the second regular session of the 90th General Assembly that would have modified the structure of any benefits provided by the state retirement plans. The Executive Order required the SRAC to ensure that any recommendations were consistent with the state's personnel management objective of promoting a benefit structure that provides financial security to state employees in an equitable and cost-effective manner. The state has adopted the following human resource objectives through the new retirement benefit structure found in the Year 2000 Plan:

a) Reducing turnover among younger employees (a career goal of 30 years of service),
b) Encouraging long service employees to retire before social security eligibility to provide promotional opportunities for younger employees,
c) Reducing payroll costs,
d) Refreshing the workforce,
e) Addressing hazardous position needs,
f) Providing for all dependents of all employee classifications in the event of duty-related death,
g) Facilitating local to state employment mobility for recruitment purposes.

The SRAC is required to furnish clear policy recommendations relating to its charge, along with other necessary recommendations pertaining to retirement, in a final report to be issued no later than September 30, 2000. The TFTC is obligated to submit to the Governor, no later than November 30, 2000, a separate addendum to the final report which contains the TFTC's recommended course of action.

For reporting purposes, the SRAC has addressed the issues related to the individual legislative proposals introduced last session under the broad captions of a) Workforce Shortage; b) Reciprocity, Portability, and Public Employee Retirement Plans; c) Benefit Equity; and d) Financial Security in Retirement. An analysis of each proposal and the subsequent findings and recommendations of the SRAC have been addressed in their respective categories.

## Evolution of Changes to the Retirement Plans

Prior to 1999, frequent amendments to the Missouri State Employees' Plan (MSEP) and the HTEHPRS' Plan resulted in a patchwork benefit structure that provided different benefits to various classifications of state employees. As a result, the state and its retirement systems were named as defendants in a number of lawsuits that claimed that certain retirement statutes had created inequities which resulted in violations of the equal protection provisions of the state and federal constitutions. These lawsuits, ultimately, resulted in the state and the retirement systems incurring significant liabilities. In 1998, the Public Safety Retirement Advisory Commission (PSRAC) issued a report that recommended a new benefit structure that would resolve the equal protection issues and other shortcomings of the existing plans. In 1999, legislation was enacted that created a new retirement plan (commonly referred to as the Year 2000 Plan or the MSEP 2000) for all state employees, thus resolving many of the internal benefit equity issues among various employee groups. The Year 2000 Plan became effective July 1, 2000.

# WORKFORCE SHORTAGE

## Overview

One of the policy goals of the Year 2000 Plan was to allow all long service employees (rule of 80 eligible) to retire with an increased benefit multiplier (1.7%) along with a temporary supplemental benefit (.8%) until social security eligibility. At that time, the formula reverts to the 1.7% factor and social security benefits are expected to replace the temporary supplemental benefit. This formula change was designed to provide a 75% income replacement ratio for employees with 30 years of service (the targeted goal described in the 1994 report of the Commission on Management and Productivity – COMAP), and to also encourage younger employees to continue in state service. (At the time the new plan was designed, general state employees, on average, retired with approximately 20 years of service and the highway patrol and Missouri Department of Transportation employees, on average, retired with approximately 30 years of service.)

In July 2000, 693 general state employees (including 257 terminated-vested members) retired under the Year 2000 Plan, versus 169 employees from July 1999. The HTEHPRS retired 134 employees in July 2000 versus 35 in July 1999. While it is believed that the Year 2000 Plan will serve as a mechanism to recruit and retain state employees at the early and mid-career stage, the number of employees leaving state employment under rule of 80 may create a temporary shortage of workers in certain agencies. This situation, combined with the lowest unemployment rate in years and, in some instances, minimal succession planning, has resulted in what many describe as a "brain drain" of experienced, qualified workers in highly competitive state classifications such as information technology and engineering.

# DROP LEGISLATION

## House Bill 2069 (HB 2069)

HB 2069, introduced by Representative Jim O'Toole, would have created a Deferred Retirement Option Plan (DROP). Specifically, this proposal would have created a forward DROP option for employees of MODOT and the highway patrol. The cost associated with the legislation was estimated to increase the HTEHPRS' contribution rate by approximately $1 to $3 million per annum the cost of which was dependent upon the outcome of employee election rates for this particular option.

A DROP is typically intended to allow an employer to keep experienced, long-term employees on staff and smooth the transitions due to retirement. Employees benefit by accruing lump sum amounts (while they continue working after becoming eligible to retire) and receive a partial lump sum distribution when they finally retire. DROPs have become more popular in recent years and are often available in police and fire plans. While discussions of a DROP at the state level have had cost neutrality as a central theme, it must be understood that such plans can be complex to administer and difficult to implement on a truly cost-neutral basis.

The narrative which follows is presented in a question and answer format and describes in detail the advantages and disadvantages of various forms of DROP designs from both the employee and employer perspective.

**Q. What is a DROP?**

A. A DROP is an optional payment form under a defined benefit plan that allows a member to receive a partial lump sum payment of his/her retirement account in addition to a reduced monthly life retirement benefit.

**Q. How many different forms of DROP exist?**

A. There are three types of DROPs commonly seen in the industry – forward DROPs, back DROPs, and Partial Lump Sum Option Plans (PLOPs, A.K.A. Actuarial Equivalent DROPs).

**Q. What is a forward drop?**

A. The member enters a DROP after eligibility for retirement, but before termination of employment. The benefit is computed and some portion is credited to an individual member account. Upon entering DROP status, the member agrees to retire within some period of time in the future. Interest may or may not be paid to the balance that is accumulating in the individual account. At actual retirement, the member receives distribution of the individual account (in a lump sum or a periodic payment) and benefit payments begin based on an amount which would have been payable had the member actually retired upon entering the DROP.

**Q. What are the advantages to the member under a forward DROP arrangement?**

A. A DROP is a means of providing for a lump sum distribution of a portion of a member's interest in a retirement plan. DROP participation may enhance the member's overall benefit value, particularly if salaries near retirement are not increasing or there is a cap on accruals. Lastly, the member can continue working in a job while effectively drawing both pension benefits and working pay at the same time.

**Q. What are the disadvantages to the member under a forward DROP arrangement?**

A. Plan benefit increases during the DROP period are generally not passed on to DROP participants and pay increases during the DROP period will not be reflected in the actual benefit at retirement. By foregoing future benefit accruals, future cost-of-living adjustments on the missing accruals are also lost. DROP participation can lead to smaller total benefit values even in some generous plans. If the DROP percentage is less than 100%, members may feel they are being penalized for participating in the program. Also by electing the DROP lump sum, the member's future pension payments will replace less of the pre-retirement income. Lastly, there are issues relating to the employee's status after electing a DROP which include how sick leave, annual leave, holiday pay, death-in-service, and disability are handled.

**Q. What are the advantages to the employer under a forward DROP arrangement?**

A. The employer has a means of offering an additional benefit choice at little or no cost provided the employer has adequately addressed the design issues associated with the program. Valuable, long-service employees may also be induced to delay their retirement thus allowing the employer more time for succession planning.

**Q. What are the disadvantages to the employer under a forward DROP arrangement?**

A. Plan administration is more complex and costly. It is also difficult to design a popular cost-neutral program. Additionally, employer payroll costs can rise if employees extend their working careers. In a period in which jobs are scarce and applicants are plentiful, an employer might lose opportunities to recruit potentially valuable new employees. There also could be the public perception issue of "double dipping."

**Q. What is a Partial Lump-Sum Option Plan (PLOP)?**

A. At the time of retirement, some portion of the benefit is distributed in a lump sum. There are various ways in which the lump sum can be determined. The periodic payment is then reduced based on actuarial calculations.

**Q. What are the advantages to the employee under a PLOP arrangement?**

A. A member's status in the system is not changed during their working career (unlike a forward DROP). A PLOP rewards members who work longer, but does not require that the retirement date be set years in advance (also unlike a forward DROP). The lump sum payment is funded by an appropriate reduction in the member's monthly benefit.

**Q. What are the disadvantages to the employee under a PLOP arrangement?**

A. Members may discover that monthly benefits remaining after the lump sum payment has been made are insufficient to meet their financial needs. Additionally, members may overestimate the amount of the lump sum payment they are going to receive (federal taxes significantly reduce lump sum payments that are not rolled over).

**Q. What are the advantages to the employer under a PLOP arrangement?**

A. The employer has a means of offering an additional benefit choice at little or no cost provided the employer has adequately addressed the design issues associated with the program.

**A. What are the disadvantages to the employer under a PLOP arrangement?**

A. The potential exists for adverse selection that could harm the retirement system on a long-term basis. Furthermore, PLOPs are actuarial assumption and age dependent – thus individuals in different plans who have the same benefit structure, salary history, and service credit could receive different benefit amounts. A PLOP also does not give the employer any advance warning that certain individuals will be leaving the workforce at a specific date in the future. Lastly, PLOPs increase the complexity of benefit administration and counseling.

**Q. What is a back DROP?**

A. At actual retirement, an option is available to the member providing for the benefit to be computed as if the DROP had been elected at some previous date. For example, it could be the later of initial eligibility for retirement or five years prior to actual retirement. Under such a scenario, the member, at retirement, would elect to back drop to an earlier period and would then receive a distribution of the individual account (lump sum or periodic payment) which would have accumulated had the member elected the DROP when eligible. Recurring monthly benefit payments would then

begin based upon the benefit the member would have been receiving had retirement actually occurred at the beginning of the DROP period.

**Q. What are the advantages to the employee under a back DROP arrangement?**

A. By making the election to back DROP at retirement, the member does not have to declare his/her intentions to retire, thereby eliminating any possibility that he/she may be overlooked for promotional opportunities because of impending retirement. Also, under the back DROP arrangement, a member does not risk making a poor choice about whether to participate in a DROP because of the inability to predict the future.

**Q. What are the disadvantages to the employee under a back DROP arrangement?**

A. An employee may elect the back DROP option in order to get the lump sum cash payment even though it may not be in their best financial interest. An employee may take the lump sum, spend it imprudently and end up with a smaller, monthly benefit that does not provide adequate financial support.

**Q. What are the advantages to the employer under a back DROP arrangement?**

A. The employer has a means of offering an additional benefit choice at little or no cost provided the employer has adequately addressed the design issues associated with the program. Valuable, long-service employees may also be induced to delay their retirement, thus allowing the employer more time for succession planning. In contrast to a forward DROP, the employer also has eliminated the risk associated with a member making a poor choice and possibly suing the retirement system later as a means of retracting that decision.

**Q. What are the disadvantages to the employer under a back DROP arrangement?**

A. In contrast to a forward DROP, a back DROP does not give the employer any advance warning that certain individuals will be leaving the workforce at a specific date in the future. Poor design can result in increased cost and benefit counseling becomes more complicated than would have been the case with no type of DROP. Also, employees who are not productive may delay their retirement.

**Q. What happens to the DROP account (any kind) when the member finally retires?**

A. Typically, plans are designed to allow members to:

a) Receive a lump sum distribution of the DROP account balance and pay the appropriate taxes;
b) Roll the account balance into an eligible plan or IRA;
c) Convert the account balance to a monthly benefit to enhance the regular pension payments; or
d) Leave the account balance in the retirement system and draw down a portion monthly (or less frequently if desired).

**Q. What are the major issues that must be considered when designing a DROP program?**

A. An employer must first determine the goals and objectives to be accomplished by establishing such a program. The employer must then determine:

- What is the relationship between retirement eligibility versus DROP eligibility?
- How long may members stay in a DROP?

- How long must members stay in a DROP?
- What percent of the accrued benefit goes into the DROP?

**Q. What are the minor issues that must be considered when designing a DROP program.**

A. The employer must determine:

- What happens if the member dies or becomes disabled during the DROP period? (Forward DROP only.)
- Will the member be eligible for any benefit increases enacted during the DROP period? (Forward DROP only.)
- How will accrued sick and vacation leave be handled? (Forward DROP only.)
- Will there be interest credits on the DROP account?
- What are the options for distribution?

**Q. What does it mean when a DROP (any kind) is cost-neutral?**

A. A DROP is cost neutral if the value of benefits to be paid under the plan to all members combined is the same as the value of the benefits that would have been paid if the DROP had not been adopted. A cost-neutral DROP will result in no change in the employer's dollar contributions to the plan.

There is a common misperception that members should be able to DROP 100% of their benefit, earn market rates of return on the DROP account, and not increase costs to the system. This belief stems from the idea that if the member had not DROPPED they would have retired. Therefore, the system would have paid the benefit anyway.

It is true that if a member DROPS at the time he/she would otherwise have retired with 100% DROP credits and market rates of return, the DROP plan would be cost neutral with regard to that member. However, that is because the member is receiving the same benefits, in total, that would have been paid by the system without the DROP.

Most members, however, will not choose to DROP at the point at which they would have retired. Many of the members will choose to DROP at a point in time which precedes the time at which they would have retired. This has two important effects to the retirement system. First, the pension pay-out period is extended and, secondly, the working period over which the retirement funds are accumulated is shortened. The resulting added cost is usually only partially offset by the savings generated by freezing pension accruals. If cost-neutrality is an objective, it is usually achieved by crediting less than 100% of the accrued pension and less than market interest (generally no interest) to the DROP account.

## Findings and Conclusion on DROP

The SRAC reviewed a wide array of information on this topic including presentations from the actuarial firm of Gabriel, Roeder, Smith & Company (GRS) on the various forms of DROPs available in the public sector. GRS serves as the actuary for both MOSERS and HTEHPRS, as well as other public funds in the state of Missouri. Public testimony in support of a DROP was also provided by Lieutenant Governor Roger Wilson, Colonel Weldon Wilhoit of the Missouri Highway Patrol, the Missouri State Troopers Association, the Highway Employees' Association, and other parties that sought passage last year of HB 2069.

The inauguration of the Year 2000 Plan combined with a nationally tight job market has resulted in the state, an employer, experiencing workforce shortages in a number of key areas. Enhancing the retirement plan by providing a DROP option may induce valuable long-service employees to delay their retirement and alleviate the transitional problems state agencies may be experiencing due to these circumstances. While a DROP might also induce non-productive employees to stay past retirement, the SRAC believes that any DROP must be available to all similarly situated employees, not selected workers or job classifications. The SRAC also believes that a lump sum benefit option would be of value to employees, particularly lower paid employees who have had less opportunity to accumulate assets during their working careers. Lastly, the SRAC noted that there appears to be considerable legislative support for a DROP option, and felt it was appropriate to recommend a cost-neutral DROP design that conforms most closely to the compensation and benefit goals of the TFTC. Although it may be seen by certain individuals as running counter to some of the objectives of the Year 2000 Plan (encouraging retirement before social security eligibility), the SRAC believes that a DROP feature is consistent with the state's "attract and retain" philosophy.

## Recommendation on DROP

The SRAC further determined that a desirable DROP option for the state should meet the following goals and objectives:

- Valuable, long-service employees may be induced to delay their retirement if a DROP is available.
- A DROP should fit within the framework of the policy goals and personnel management objectives described in the Executive Order.
- A DROP may help serve as an additional recruitment and retention tool.
- A DROP may provide more flexibility to the state in serving the needs of a fluctuating workforce.
- A cost-neutral DROP would enable the state to offer an additional benefit choice at little or no cost, however, care should be taken to develop an option that will not promote the perception of "double-dipping".
- A DROP should not be so complex or difficult to administer that information cannot be easily communicated to members.
- A DROP should enable employees to receive a lump distribution at time of retirement, however, should be structured in such a fashion as to prevent employees from making a poor choice.

A DROP subcommittee was subsequently formed to review the various DROP alternatives and make a recommendation to the SRAC regarding which DROP options should be considered. After extensive analysis and review, the DROP subcommittee recommended a cost-neutral back DROP design that resolved many of the issues associated with the forward DROP and PLOP options. The SRAC subsequently endorsed the cost-neutral back DROP design that appears on the following page for consideration by the TFTC.

## PROPOSED BACK DROP MODEL

**Members Covered:**
All members retiring under chapter 104 RSMo, other than elected officials and members of the general assembly. Applies to members retiring under both MSEP[1] and MSEP 2000.

**Members Eligible:**
All members who continue in service for at least two years beyond their earliest eligibility for unreduced age and service retirement. At retirement it will be determined whether they are eligible for the back DROP under MSEP, MSEP 2000, or both.

**Timing of DROP Election:**
At separation from service.

**DROP Period:**
The shorter of the period beginning upon reaching earliest eligibility for unreduced age and service retirement and ending at separation from service, or the period beginning five years before separation from service[2].

**Computation of DROP Amount:**
The benefit is computed as if the member elected the DROP at the beginning of DROP period and chose the desired form of payment (normal annuity or survivor option) at that date. The DROP account balance is computed as if 90% of the benefit otherwise payable (including COLAs on benefits that would have been paid if the member had retired at the beginning of the DROP period) had been paid to the DROP account during the DROP period. No interest is credited to DROP accounts.

**DROP Balance Distribution Options:**
Payment in a lump-sum at separation from service, or rollover to IRA.

**Examples of Eligibility:**

MSEP[3]
Rule of 80 eligibility plus 2 years
Age 62 with 17 years service (60 & 15 + 2 years)
Age 67 with 6 years of service (65 & 4 + 2 years)

MSEP 2000
Rule of 80 eligibility plus 2 years
Age 64 with 7 years service (62 & 5)

In order to achieve the SRAC goal of cost-neutrality, the actuary determined that DROP accounts could only be credited with 90% of the benefit otherwise payable during the DROP period, regardless of the plan elected.

[1] MSEP refers to MOSERS and HTEHPRS' closed plans.
[2] The DROP period may differ depending on whether is it under the MSEP or MSEP 2000.
[3] For highway patrol and water patrol members retiring under the MSEP, the life benefit is increased by one-third and the normal form of payment is an unreduced joint & 50% survivor option.

## Recommendation on DROP

To recap, the SRAC determined that valuable, long-service employees could possibly be induced to delay their retirement if a DROP was added to the current menu of retirement options, thus affording state agencies the opportunity to further enhance their succession planning efforts, and ease the transition problems associated with retirement. If the TFTC is supportive of this conclusion, the SRAC recommends that legislation be drafted and introduced that would make the proposed back DROP model available to members retiring under Chapter 104, RSMo (other than elected officials and members of the general assembly).

# RECIPROCITY, PORTABILITY, AND PUBLIC EMPLOYEE PLANS

## Overview

The term portability describes retirement plan provisions that allow an individual employee to move from one employer to the next without any significant impairment of the pension benefits that are being accrued.

One of the policy goals of the Year 2000 Plan was to facilitate local to state employment mobility for recruitment purposes. Specifically, the Year 2000 Plan contains a provision that allows service earned with another employer to count toward state retirement benefits under certain circumstances. The rationale behind this provision was based on the premise that the state benefits if it provides a mechanism that allows for the recruitment of talented, experienced employees from the public sector. This provision contained some restrictions – an employee must work at least ten years with the state before vested local government service is recognized, and the transferring system must agree to transfer an amount equal to the liability the transferring system carries for that individual. In exchange for the transfer, the employee receives full credit for service earned under the transferring system. Prior to the enactment of this benefit change, only limited provisions existed that allowed general employees to move among state agencies covered by MOSERS and HTEHPRS without negatively impacting their retirement benefits. More restrictive provisions also exist under Chapter 105, RSMo that allow employees to move from local government positions to state agencies, but these provisions are rarely used because of the employee cost associated with purchasing such service. (See Exhibit A that describes in detail the portability provisions that exist among the public employee retirement plans in Missouri.)

The state's regional colleges and universities have long maintained that the current defined benefit plan's lack of interstate portability discourages some job candidates from taking positions with Missouri colleges. This issue, coupled with their faculty's familiarity with, and desire to have, Teachers Insurance Annuity Association -- College Retirement Equity Fund (TIAA-CREF) products, has resulted in Optional Retirement Plan (ORP) legislation being introduced in the General Assembly six times since 1992. (In 1992, ORP legislation was truly agreed to and finally passed; it was, however, subsequently vetoed by Governor Ashcroft.)

# ORP LEGISLATION

## House Bill 1660 (HB 1660)

The most recent proposal, HB 1660 introduced by Representative Don Summers, would have allowed each of the regional colleges and universities to establish an ORP for all full-time teaching and senior administrative personnel. Under this proposal, all future employees of the institutions would have been allowed to elect participation in an ORP in lieu of participating in MOSERS. Participation also would have been extended to current employees of MOSERS who were appointed to ORP eligible positions subsequent to the effective date of the act.

## Philosophy

Historically, the state's policy objective has been to make use of its defined benefit plan to both attract and retain quality employees. A defined benefit plan is consistent with this objective since the benefit that is paid at retirement is based upon salary near time of retirement and total state service. The defined benefit plan currently in place for state employees allows the state to:

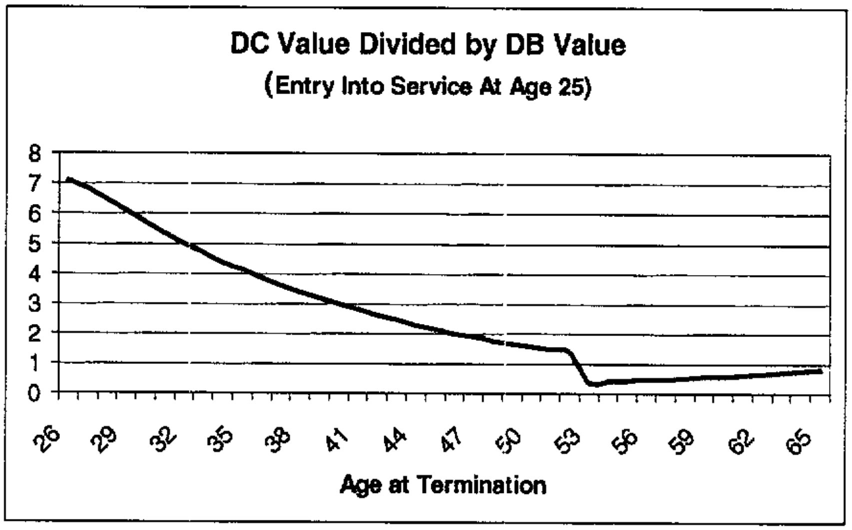
- Attract and retain quality employees;
- Be competitive with other employers;
- Assure that retiring workers have a base level of retirement income in relation to the amount of service rendered;
- Allow older workers to move out of the workforce with financial dignity;
- Encourage older, long-service workers to leave the workforce;
- Address the financial needs of employees who leave the workforce as the result of a casualty event; and
- Keep retired workers off the welfare rolls.

Conversely, a defined contribution plan provides a benefit based solely on the amount contributed to an individual account plus any gains or losses that may be incurred through investment of account balances. An ORP actually facilitates short service since its plan design enables employees to move without incurring disadvantages (financial losses) in benefit plans – thus employees have no significant benefit related incentive to stay with an employer.

## Change in Policy Objectives

There is no question about the fact that the state's defined benefit plan works to the advantage of employees who are relatively young when hired and who continue in service with the state until reaching eligibility for an immediate benefit at termination of state employment. In contrast, a defined contribution plan generally works to the advantage of employees who terminate their service before being eligible for an immediate benefit.

The charts that follow illustrate the magnitude of the differential in benefit value. The values used in preparing the charts are based on the benefit accrued under the Year 2000 Plan compared with the values which would accrue in a defined contribution plan with contributions equal to 7% of pay and earnings of 8% per year. In both cases, it was assumed that pay would increase at the rate of 4.5% per year. These charts were prepared assuming various ages at date of hire (25, 35, and 50) and show the defined contribution value relative to the defined benefit value at any point of termination between date of hire and age 65. A value greater than 1 indicates that the defined contribution plan benefit has a higher value at termination than the defined benefit plan benefit at that same point in time. (A change in assumptions about the two plans would change the magnitude of the differences but not the general direction.)


DC Value Divided by DB Value
(Entry Into Service At Age 25)
8
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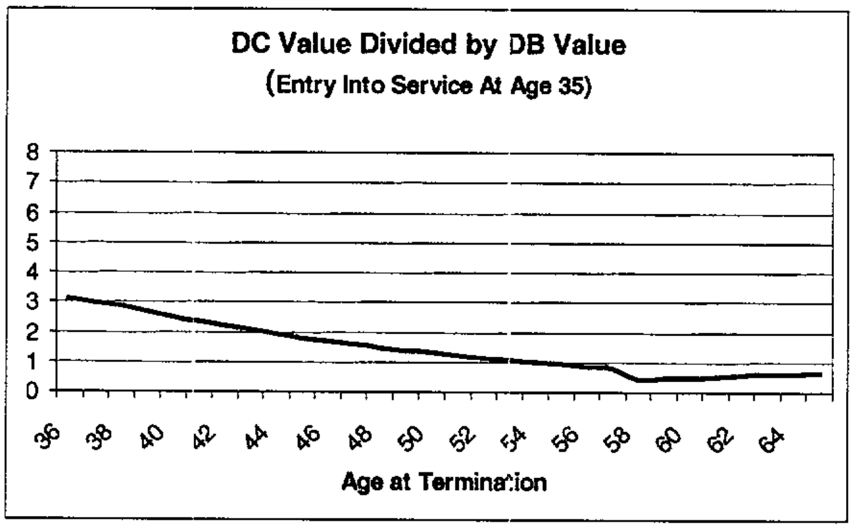
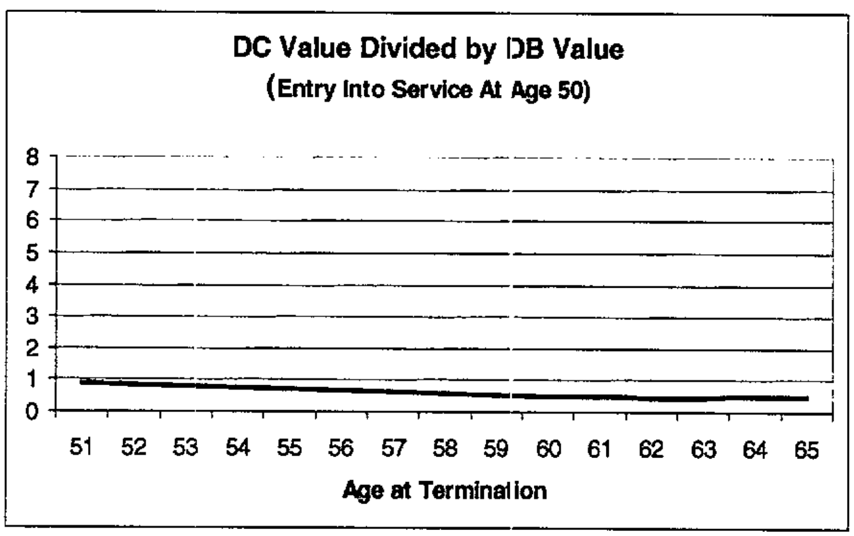
Age at Termination


DC Value Divided by DB Value
(Entry Into Service At Age 35)
8
7
6
5
4
3
2
1
0
36
38
40
42
44
46
48
50
52
54
56
58
60
62
64
Age at Termination


DC Value Divided by DB Value
(Entry Into Service At Age 50)
8
7
6
5
4
3
2
1
0
51
52
53
54
55
56
57
58
59
60
61
62
63
64
65
Age at Termination

If a defined contribution alternative is made available to employees, a number of the policy objectives inherent in the design of the existing plan would need to be abandoned. For example, a defined contribution plan will not:

- Encourage workers to continue in service with the state.
- Assure that retiring workers have a base level of retirement income in relation to the amount of service rendered.
- Encourage older long-service workers to leave the workforce.
- Address the financial needs of employees who leave the workforce as the result of a casualty event.

## Where Have All the Gains Gone?

Defined contribution plan advocates frequently suggest that investment gains in defined benefit plans do nothing to help the plan participants because they simply serve to reduce the employer's contribution rate. A review of the facts in Missouri will reveal that the legislature and administration have passed substantial portions of MOSERS' investment gains on to plan participants by way of benefit increases. For example:

Since inception:

- The basic benefit formula has more than doubled.
- Required member contributions of 4% of pay have been eliminated.
- Vesting has been reduced from 15 to 5 years.
- The final average salary period has been reduced from five to three years.
- A statutory guaranteed annual COLA provision has been added to the plan.
- The plan's death-in-service benefits have been expanded dramatically.
- "Rule of 80" eligibility has been added to allow earlier retirement for career employees.
- A temporary benefit for those eligible for "Rule of 80" retirement has been added to serve as a bridge payment until social security benefits are available.

It is unlikely that these and other benefit increases would have been possible had it not been for the success the plan has experienced in the investment markets. The state could have used the plan's investment gains to dramatically reduce the contribution rate. However, the state has effectively made a commitment to a level contribution rate and passed investment gains along to members through benefit increases such as those identified above. Of course, these changes are primarily to the benefit of those employees who continue in state service until eligible for retirement benefits upon termination (as should be expected of a plan targeted at employee retention).

## Fundamental Question

The fundamental question facing the state is whether or not it should deviate from the "attract and retain" philosophy imbedded in the existing retirement plan and, as a consequence, facilitate employee movement to other employers. In an effort to fully address this question, the SRAC heard presentations on a number of approaches which might be used to facilitate portability and/or give employees options regarding the retirement arrangement which they believe may be best suited to their individual circumstances. With the exception of the first one listed, under each of these alternatives, MOSERS would be responsible for administration.

## Alternative Plan Designs to Facilitate Portability

The first alternative involved allowing individual employees to elect to have some stipulated amount directed, on their behalf, to individual accounts with organizations like TIAA-CREF and Variable Annuity Life Insurance Company (VALIC). These contributions would be in lieu of the state's contribution to MOSERS, and the employees participating in the optional retirement plan would direct how the funds are invested. If this approach were to be followed, it would probably be prudent to extend its availability to all employees and not just to higher education employees. The rationale for making it universally available is to eliminate potential equal protection issues that might otherwise need to be addressed at a later date.

## ALTERNATIVE TO TRADITIONAL OPTIONAL RETIREMENT PLAN

The following describes an alternative to the ORP that would allow for establishment of individual account balances and management thereof by participants yet also allows for participation in the state's defined benefit plan.

**Eligibility for Participation:**
Member is eligible after 5 years of service covered by MOSERS' defined benefit plan.

**Creation of Member's ORP Account:**
After a member elects to participate in the ORP, the state contributes 3.5% of the member's pay to an individual account. That account will receive investment income credits based on the asset mix of the member's choice (as described later). 3.5% is approximately ¼ of the contribution that is being made for the Year 2000 Plan – the basic defined benefit plan.

**Changes:**
Annually, before and after separation from service.

a) A member elects to be covered by the ORP – for indefinite future, unless changed at annual anniversary date.

b) Investment of ORP contributions would be in one of the asset allocation mixes provided by MOSERS. To illustrate:

| | A | B | C |
|---|---|---|---|
| Bonds | 50% | 75% | 25% |
| Stocks | 50% | 25% | 75% |

Investment results would be based on indexes rather than MOSERS' actual returns. An age based default election could be established for the various funds.

**Effect on Basic Benefits When Member Elects to Participate in ORP:**
Eligibility for basic benefit is not changed. The amount of the basic benefit is reduced to 75% for the period(s) of time when ORP contributions are being credited to the member's account.

To illustrate, if a member had 25 years total service credit, including 15 years of ORP coverage, the basic defined benefits would be computed as if the member had 21.25 years of service credit (10 years @ 100% plus 15 years @ 75%) – ORP benefits would be in addition to the defined benefit plan benefits. (Actual service could be considered for rule of 80 eligibility.)

By electing to participate in the ORP, a member adds a third major factor to the determination of the amount of MOSERS' benefits – investment return. Basic defined benefits continue to be predicated on pay and years of service.

**What Happens When Covered Service Ends and When Monthly Retirement Benefits Become Payable?**

**Basic Benefits** are initially determined by applying specified formulas to years of service and final average pay. The initial amount is adjusted annually after benefit commencement to reflect a portion of inflation.

**ORP Benefits** are adjusted annually by the investment return attributed to the member's ORP account during the past year.

**Additional Demands on MOSERS' Administrative Staff:**

The basic workings of the investment world will have to be explained to members so that they can make informed decisions about ORP participation. The mid-career program would need to be expanded to be available to all members.

Inevitably, bear markets appear. These low or negative results will provoke irrational negativism from some members. Staff will need to be prepared to deal with this situation.

No increase in contribution dollars would be necessary under this proposed alternative.

## INDEX DEFERRED BENEFITS ALTERNATIVE

The primary shortcoming of traditional defined benefit plans according to defined contribution advocates is that they base benefits on pay at or near time of separation from service. Accordingly, employees who leave relatively early in their careers lose significant value by virtue of the fact that inflation (and possible merit increases in salary) between termination of employment and the benefit effective date are not considered in determining benefit amounts.

One possible way to address this situation would be to index vested deferred benefits for inflation (or some portion thereof) between the termination date and benefit effective date. Under such a scenario, the employer could:

- Establish a minimum service requirement (longer than the 5-year vesting requirement) for indexing eligibility.
- Finance indexing by establishing a reserve using some portion of income in excess of the actuarially assumed rate.
- Establish a maximum annual index figure equal to the lesser of (i) the amount which can be financed by available reserves or (ii) the average increase in pay for active state employees (which includes the possibility of a zero amount).

Such provisions for indexing would have the following advantages:

- By having a minimum service requirement for eligibility (such as ten years), it would provide a considerable incentive for employees to continue in service with the state for at least that long. Once past the 10-year barrier, many employees will decide to make a career of state service.

- By financing the provision with income in excess of the assumed rate, there would be no immediate increase in the contribution rate. (This means that in the future there will either be less in the way of reductions in the employer contribution rate and/or less available to provide other benefit increases.)

- The maximum would assure that terminated-vested employees do not receive increase amounts greater than warranted by increases in active member pay.

In addition, this indexing approach versus establishment of a defined contribution optional retirement plan, assures that:

- The amounts available are applied to retirement income (versus the possible cash-out under a defined contribution plan).

- Less of the state's contributions would end up as part of administrative expenses, meaning that more of the contributions would go toward benefits.

Furthermore, employees who have a legitimate need to leave state employment after several years of service could do so without sacrificing a significant portion of their retirement income.

The downside of indexing deferred benefits is the perception that the state would be funding benefits for employees who are no longer in service.

## CASH BALANCE ADD-ON APPROACH

Under this approach, a phantom account would be maintained for each employee. To that account would be credited an amount equal to X% of pay and the balances in that account would be assumed to earn interest at the rate of Y%. (The values of X and Y would need to be stipulated in the plan.) A minimum vesting period (like five years) could be established before employees would be eligible for any benefit under this arrangement.

Upon separation from service prior to retirement eligibility, the member would be eligible for a lump-sum payment equal to the accumulated account balance. Alternatively, such a terminated-vested member could leave the account balance and let it accumulate value during the deferral period.

At the time of eligibility for retirement, the amount of the benefit would be determined as the greater of the benefit based on the regular benefit formula or the annuity which could be purchased (based on stipulated assumptions) using the balance in the phantom account.

The Cash Balance Add-On Approach would result in an increase in required contributions because it would increase the value of benefits otherwise payable to short service employees. (It is worth noting that a Cash Balance feature was recently included in the retirement plan maintained for employees of the University of Missouri.)

## Testimony in Support of an ORP

Public testimony in support of an ORP was provided by Dr. Jack Macgruder, President of Truman State University; Dr. Rick Althaus of the Faculty Senate; and John Black, General Counsel for Southwest Missouri State University. Representatives of TIAA-CREF also testified in support of an ORP for the regional colleges and universities. These individuals maintain that:

- Some professors and administrators considering employment in Missouri have refused to continue discussions when they learn that no ORP is available (although no statistics supporting this position were presented).
- Institutions must negotiate higher salaries to recruit desired staff to offset the lack of availability of an ORP (although no statistics supporting this position were presented).
- Institutions cannot be competitive with industry peers (their statistics state that there are over 1,000 public institutions in 45 states across the country that offer ORPs).
- Encouraging older workers to retire by offering a defined benefit plan is not necessarily a goal of the higher institutions as many professors and administrators are productive in their advanced years.
- In the event of a participant's death, the full account balance is paid to the estate (in contrast to the survivor benefits offered by the state's defined benefit plan).

## Issues With Previous ORP Designs

One of the issues associated with previous ORP proposals stems from equal protection concerns. To elaborate, the state and the TFTC have, in the past, consistently been concerned with singling out a relatively highly compensated contingent of state government employees and allowing them to have benefit alternatives that are not available to other rank and file employees. The state's past experience (four equal protection lawsuits with settlements totaling over $100 million) suggests that pressure would ultimately mount to extend the provisions to other classifications of employees. The end result of such activity could require the state to extend participation in an ORP to all of MOSERS' membership and that, in turn, could create a destabilizing effect on the defined benefit plan through adverse selection. The state would also be required to abandon the "attract and retain" philosophy currently set forth as a personnel management objective.

Regardless of the size of the group eligible for the ORP, it would be reasonable to assume that most eligible participants would select the plan providing the greater economic value and thus the greater cost (adverse selection). Assuming that new hires act rationally, the younger ones will elect the ORP and the older ones will elect MOSERS. Over a period of time, this will have the effect of (a) increasing the average entry age and (b) decreasing the active population participating in MOSERS, both of which will lead to escalating costs. Contribution rates for MOSERS will increase because the normal cost is based on entry age (the older the entry age the higher the rate) and because the declining membership will initially behave like a closed group. Thus, the end result would be an increase in the contribution rate required to support MOSERS.

Another issue associated with past ORP designs is the election to opt out of the defined benefit plan. The history of "one-time irrevocable elections" is that, in practice, they turn out to be neither. Since employees do not know what the future economic environment or their employment status will be, almost invariably, the charge is heard later that the choice was not adequately explained. Pressure

builds and eventually another (and sometimes a third and fourth) election is permitted. When this occurs, additional cost is incurred to support the "best of both worlds" environment.

## Findings and Conclusion on ORP

After much discussion, the SRAC determined that establishing an ORP for the regional colleges and universities would run counter to the "attract and retain" philosophy that has been promoted by the state and endorsed in the Year 2000 Plan. The SRAC believes that an ORP may actually facilitate short service since its plan design enables employees to move without incurring any financial loss in benefit plans. As a result, employees have no significant benefit related incentive to stay with an employer. The state's defined benefit plan is based on salary and service and it allows the state to:

- Retain quality employees;
- Assure that retiring workers have a base level of retirement income in relation to the amount of service rendered;
- Encourage older long-service workers to leave the workforce, and
- Address the financial needs of employees who leave the workforce as the result of a casualty event.

If an ORP is made available to all state employees, these policy objectives would have to be abandoned.

The alternative approaches previously described in this report (Alternative To Traditional Optional Retirement Plan, Indexing Deferred Benefits, and the Cash-Balance Add-On Approach) were not favorably received by the proponents testifying in favor of ORP legislation. This is, in part, due to the fact that several of the alternative approaches would be administered by MOSERS in lieu of an outside administrator (an organization like TIAA-CREF or VALIC), and the university administration and faculty's familiarity with, and desire to have, a TIAA-CREF like product.

Although the colleges and universities maintain that that the current defined benefit plan's lack of portability discourages some job candidates from taking positions with Missouri colleges, particularly short-term recruits, that can also be said for all state agencies. Take, for instance, cabinet level members who typically serve no more than eight years in an administration, or employees who are only needed for the short-term in the fields of technology or engineering who will not meet the 5-year vesting requirement of the state's defined benefit plan.

That being said, the SRAC also recognizes that ORP legislation has been introduced in the General Assembly a number of times during the past decade and there is considerable support for an ORP in the legislature. If it is determined that faculty and senior administrative personnel of the colleges and universities truly have different needs than other state agencies, then the SRAC recommends the following plan design:

## University Retirement Plan (URP)

- Establish a defined contribution plan with immediate vesting for faculty and senior administrative personnel at the regional colleges and universities who are hired after the effective date of the legislation. There would be no option – all qualifying personnel would automatically participate in the defined contribution plan. (Since it is not needed to attract employees who are already there, it should not be extended to the present population.)

- Establish a defined contribution employer contribution rate equal to 1% less than the normal cost rate established for the regional college and university employees who participate in MOSERS. This would allow for the financing of additional casualty benefits which would not be available to these employees through MOSERS and would provide some allowance for potential contribution rate increases for the group. (In this regard, it is anticipated that regional colleges and universities would be considered one employer group for contribution rate determination purposes. Thus their MOSERS' rate and their defined contribution rate would vary from year to year based on their collective experience.)

- Responsibility for selecting an outside service provider and investment vehicles for the defined contribution plan should be assigned to the MOSERS' Board of Trustees.

This approach should:

- Address the putative special needs of the regional colleges and universities.

- Eliminate the marketing conflicts that materialize with an ORP.

- Preclude employees from making what they later determine to be a bad choice regarding the plan in which they elect to participate.

- Assure that the plan is administered in the most cost-effective manner possible and restrict any potential adverse selection to the regional colleges and universities.

- Eliminate most of the "me too" demand for options that might arise among other employee groups if an ORP were established just for the regional colleges and universities.

## Recommendation on ORP

To recap, the SRAC believes that that establishing an ORP for the regional colleges and universities would run counter to the "attract and retain" philosophy that has been promoted by the state and endorsed in the Year 2000 Plan. However, the SRAC also recognizes that considerable legislative support for an ORP exists in the General Assembly. Given this situation, the SRAC would recommend the proposed university retirement plan (URP) previously described. The URP approach would address most of the problematic design issues associated with past ORP proposals – specifically, those concerns that deal with equal protection, adverse selection, and irrevocable elections.

# BENEFIT EQUITY

The TFTC has adopted a compensation policy statement which reads, in part, as follows: "To recruit, retain and pay employees who provide the highest quality services to the citizens of the state, the state employee benefits structure, combined with appropriate pay, should provide financial security to employees in an ***equitable*** and cost-effective ***manner (emphasis added)***." This policy statement further specifies certain goals that encourage the State of Missouri to:

- Create a comprehensive benefits package that is ***externally competitive*** with the marketplace, and that is ***internally equitable*** (***emphasis added***).

- Allow ***career*** state employees to maintain a ***reasonable standard of living at retirement*** through a combination of ***equitable defined benefit***, social security and individual tax-favored savings plans (***emphasis added***).

- Eliminate ineffective duplication of benefit plans.

## PUBLIC SAFETY LEGISLATION

### Senate Bill 863 (SB 863) and House Bill 1914 (HB 1914)

Last session, SB 863 and HB 1914, introduced by Senator Harold Caskey and Representative Wayne Crump, respectively, would have provided uniformed conservation agents (both active and terminated-vested employees), retirees, and survivors with an additional 33.3% retirement benefit in the Missouri State Employees' Plan (MSEP). This legislation was prompted by provisions in the closed plan that allow uniformed employees of the highway patrol and water patrol covered by that plan to become eligible for retirement benefits that are one-third greater than benefits for non-uniformed employees. This perceived inequity has resulted in other classifications of employees, such as the uniformed conservation agents, attempting to make the case that they should also be considered for a higher level of benefit.

The Public Safety Retirement Advisory Commission (PSRAC) issued a report in 1998 that specifically dealt with benefits for public safety officers. One of the primary tasks of the PSRAC was to determine which, if any, classifications of state employees should be given a "public safety" designation and consequently participate in a retirement arrangement which is different from the plan for general employees.

The PSRAC determined that the initial rationale for the higher benefit level for uniformed employees of the highway and water patrol no longer made a persuasive case for the existing benefit design, and the extra 33.3% retirement benefit was not incorporated into the Year 2000 Plan.

## <u>House Bill 1665 (HB 1665) and Senate Bill 813 (SB 813)</u>

Other public safety legislation introduced this year (HB 1665 introduced by Representative Chuck Pryor) would have provided a burial benefit not to exceed $10,000 and a death benefit in a lump sum of $50,000 to certain public safety officers killed in the line of duty. Although this legislation originally did not address state employees, it was later amended to include certain positions that fall within the department of public safety. Similar legislation was subsequently amended into a House Committee Substitute for SB 813 that would have increased the proposed lump sum death benefit to $100,000, and the definition of a public safety employee would have been further expanded to include the state classifications of developmental aide, psychiatric aide, and security aid.

The PSRAC found that it was not feasible to craft a workable definition of a "public safety" employee, since there are so many classifications of employees that might be included under such definition, and because the cost to continually fund benefit increases to such an open-ended group would prove too costly. (A sampling of these groups might include the Capitol Police, Conservation Officers, Corrections Officers, Gaming Commission Enforcement Personnel, Highway Patrol, line employees of the state Fire Marshall, line employees of the Juvenile Court, Probation and Parole, Liquor Control Officers, Park Rangers, select employees of the Adjutant General, Water Patrol, Campus Police/Security, Criminal Investigators, Bailiffs, etc.)

The PSRAC was also concerned that singling out a select group of employees for special benefits without clearly defining the criteria for such treatment would result in equal protection lawsuits being filed against the state by other rank and file employees. SB 863 and HB 1914 were both designed to single out state conservation agents for special treatment.

In recent years, the state has paid out more than $100 million in benefits as a direct result of equal protection lawsuits that have been filed by various groups of state employees. It is important to note that the most recent equal protection lawsuit related to conservation employees receiving the joint & 50% survivor benefit at no cost, while other state employees were required to take reductions in benefits. This particular benefit inequity resulted in the state paying an increased contribution rate of 1.52% of payroll which, in the first year, resulted in an increase in contributions of $19 million. (That amount will increase for a number of years in the future as payroll increases.) In addition, lump sum payments totaling approximately $11.5 million were made.

HB 1665 and SB 813 also singled out certain groups of public safety employees and would have allowed them to have additional death and burial benefits that are not afforded to other state employees. As stated previously, the state's past experience suggests that pressure would ultimately mount to also extend the provisions of this act to one or more of the other groups previously identified. This point is further illustrated by the amendment to the House Committee Substitute for SB 813 that expanded the definition of a public safety employee to include the state classifications of developmental aide, psychiatric aide, and security aide.

The PSRAC adequately addressed the issues of employer responsibility for duty-related death for <u>all</u> state employees by providing a 50% percent of pay minimum death benefit and expanding the state's basic life insurance coverage to include triple indemnity provisions. Last session, those life insurance provisions were further enhanced when the basic life coverage of $15,000 was increased to one-times salary (with a $15,000 minimum). This new coverage becomes effective January 1, 2001 and will provide a triple indemnity benefit that is equivalent to three-times annual salary in lieu of the present benefit of $45,000.

## Findings and Conclusion on Public Safety Legislation

Testimony was offered from various public safety groups that expressed their interest in having the extra one-third incorporated into both the old and new plans so that existing employees and new hires would be treated the same. However, the SRAC came to the conclusion that no new information existed that gave sufficient reason to deviate from the PSRAC's original findings and conclusion on this issue. Further, the SRAC believes that the state has adequately addressed the issues of employer responsibility for duty-related death by providing a 50% percent of pay minimum death benefit and expanding the state's basic life insurance coverage to include triple indemnity provisions and increased basic coverage amounts.

## Recommendation on Public Safety Legislation

The SRAC believes that the issues associated with offering separate benefits for public safety employees have been sufficiently and thoroughly explored by the PSRAC, and resolved through the enactment of the Year 2000 Plan which does not differentiate in benefit levels for general employees and public safety like classifications. The SRAC voted not to support the additional one-third retirement benefit for conservation agents and special death and burial benefits for state public safety employees.

# PUBLIC SERVICE COMMISSION LEGISLATION

## House Bill 2090 (HB 2090)

HB 2090, legislation sponsored by Representative Mary Hagan-Harrell, would have transferred regulatory law judges appointed by the Public Service Commission from MOSERS' General Employee Plan to the Administrative Law Judges' and Legal Advisors' Plan (ALJLAP).

Under this proposal, regulatory law judges would have been covered by the ALJLAP that offers a formula of 4.17% per year, up to 50% with 12 years of service, in lieu of being covered by the closed General Employee Plan which offers a 1.6% benefit multiplier; or under the Year 2000 Plan which offers a 1.7% benefit multiplier and a temporary benefit multiplier of .8% (for those retiring under Rule of 80).

Membership in the ALJLAP is currently available to an administrative law judge (ALJ) or legal advisor in the Division of Worker's Compensation, a member or legal counsel of the Labor and Industrial Relations Commission, the Chairman of the State Board of Mediation, or an administrative hearing commissioner.

To provide some history, the ALJLAP was created in 1984 and membership was only extended to administrative law judges. In 1987, membership was expanded to include the Labor and Industrial Relations Commission. The Chairman of the State Board of Mediation was added a year later, and in 1994 membership was expanded to include legal counsel for the Division of Labor Standards. In 1997, administrative hearing commissioners were included.

## Findings and Conclusion on HB 2090

Benefit disparity exists in the ALJLAP because the membership has grown to include the previously mentioned groups without the benefit of a clear definition of position characteristics required for

eligibility in the system. As illustrated in the table that follows, the criteria for membership in the ALJLAP appears to be inconsistent and incompatible with the state's previously stated policy objectives concerning benefit equity.

| Classification | Definition |
|---|---|
| Worker's Compensation ALJ | ➢ Must be a licensed lawyer;<br>➢ Cannot practice law while holding office;<br>➢ Appointed by the Division of Worker's Compensation;<br>➢ No terms and are removable by the governor per performance review;<br>➢ Jurisdiction to hear and determine claims upon original hearing, however, no review jurisdiction;<br>➢ May approve settlement contracts; and<br>➢ Must have specialized training. |
| Legal Advisors | ➢ Not required to be an attorney;<br>➢ No terms;<br>➢ May approve settlement agreements;<br>➢ Jurisdiction to hear and determine claims upon original hearing;<br>➢ Act in the capacity of associate ALJ; and<br>➢ Must have specialized training. |
| Chairman of the Board of Mediation | ➢ Must devote full-time to duties of office; and<br>➢ Appointed by the governor w/advice & consent of senate. |
| Labor and Industrial Relation Commissioners | ➢ Must reside in state for at least 5 years prior to appointment;<br>➢ Appointed by governor w/advice & consent of senate; and<br>➢ One of the three members must be an attorney. |
| Administrative Hearing Commissioners | ➢ Appointed by governor w/advice & consent of senate;<br>➢ Six-year terms;<br>➢ Must be an attorney;<br>➢ May not practice law during term of office;<br>➢ May conduct hearings, make findings of fact and conclusions of law; and<br>➢ May approve settlement. |

To illustrate the wide disparity in job descriptions, a legal advisor in the Division of Worker's Compensation is not required to be an attorney, yet may approve settlement agreements and has the jurisdiction to hear and determine claims upon original hearing. Conversely, an administrative hearing commissioner must be a lawyer, is appointed by the governor with the advice and consent of the senate, and is appointed to serve a six-year term. While the Chairman of the Board of Mediation is appointed by the governor with the advice and consent of the Senate, the only qualification is that he/she must devote full-time to the duties of office. Regulatory law judges may also conduct hearings,

however, may not issue a binding rule without commission approval. The common denominator appears to be that employees holding these positions have the authority to preside over hearings.

Given the lack of defined criteria for membership in the ALJLAP, other groups of employees (such as regulatory law judges) serving in somewhat similar positions have sought legislative support for adding additional classifications to the system. Without a clear definition, it is likely that additional piecemeal solutions will be addressed legislatively (resulting in more disparity), and the state could be exposed to equal protection lawsuits from other groups of employees who consider themselves similarly situated. A sampling of these groups might include hearing officers employed by the Department of Insurance, the Department of Natural Resources, the Department of Health, the Department of Mental Health, the Missouri Commission on Human Rights, the Department of Revenue, the Department of Social Services, the Missouri Gaming Commission, the Department of Agriculture, the State Tax Commission, the Highway and Transportation Commission, the Personnel Advisory Board, the Division of Employment Security, the Department of Public Safety, etc. A further complication is that many of the employees who act as hearing officers for these agencies only do so on a part-time basis – the balance of their time is spent on duties not related to hearings.

The SRAC heard testimony from the PSC regarding the complexity of duties associated with the regulatory law judge position and the high turnover rate experienced in that department. Information provided by the PSC states that regulatory law judges are among the lowest paid in the country and are the lowest paid in the Midwest. While the PSC has undertaken a pay plan that should provide some immediate relief from the exodus of experienced regulatory law judges who are leaving state government to go to the private sector, they believe that expanding membership in the ALJLAP to include regulatory law judges would help resolve their retention problem.

The SRAC found this situation to be very similar to the public safety issue. Given the absence of defined criteria for membership in the ALJLAP, the lack of a rational basis for having a separate retirement plan such as the ALJLAP, and the number of positions that could potentially be eligible for inclusion in the ALJLAP, the SRAC was faced with the same philosophical issue – that is, which, if any, classifications should be eligible for membership in the ALJLAP. Is this issue resolved through expansion, limitation, or elimination of the ALJLAP in the future? Further, is the retention issue facing the PSC any different than that facing other state agencies in a highly competitive and tight labor market?

## Recommendation on HB 2090

The SRAC was unable to adequately explore and resolve these issues due to time constraints and the number of other complex legislative retirement proposals that the SRAC was charged with evaluating. However, the SRAC recommends that the criteria for membership in the ALJLAP be carefully examined and clarified in order to avoid future litigation. Items for consideration might include term limits or recruitment late in an employee's career versus denominators that are common throughout state government. The SRAC also recommends that a separate commission be appointed to further evaluate the criteria for membership in the ALJLAP and to determine whether or not sufficient evidence exists to expand, limit or contract membership in the system in the future.

# FINANCIAL SECURITY IN RETIREMENT

At the time the TFTC adopted its benefits policy statement, it also addressed specific goals that related to financial security in retirement. These goals, in part, encouraged the State of Missouri to:

- Implement a flexible benefits package that provides employees with options for meeting their individual and family needs, and yet assures that ***basic levels of health care*** and ***retirement coverage will be maintained (emphasis added).***
- Ensure ***equitable employer contributions for health care coverage for state employees, retirees, spouses and other dependents*** that assures high quality care in a cost effective manner.
- Allow ***career*** state employees to maintain a ***reasonable standard of living at retirement*** through a combination of ***equitable defined benefit***, social security and ***individual tax-favored savings plans*** (***emphasis added***).

## FORMULA INCREASE LEGISLATION

### House Bill 1847 (HB 1847)

HB 1847, introduced by Representative Bill Skaggs, would have increased the current benefit formula in the closed plans that are administered by MOSERS and HTEHPRS from 1.6% to 1.7% for all active, terminated-vested, and retired members. The cost of this proposal was estimated to be approximately $21.4 million per annum.

To provide some background, the Year 2000 Plan was crafted to address several benefit inequities in the closed plan and also to incorporate features that promote the state's personnel objectives.
The Year 2000 Plan offers <u>all</u> state employees and retirees a benefit formula that is based on a 1.7% multiplier, and also includes a temporary benefit of .8% until age 62 for members retiring under rule of 80 (total formula 2.5%). This structure was designed to reduce turnover among younger employees and allow retirement before social security eligibility. All current active members, terminated-vested members, and retirees will be given the opportunity to elect to participate in the new retirement plan which became effective July 1, 2000.

### Findings and Conclusion on HB 1847

While the benefit formula was increased in the Year 2000 Plan, certain features presently available in the closed plan were eliminated as a cost reduction to offset the costs associated with the increased multiplier and temporary benefit. One such benefit was the unreduced joint and survivor option. This particular option was not included so that the value of benefits could be determined without regard to marital status (although reduced survivor options are available). In regard to cost-of-living adjustments (COLAs), the Year 2000 Plan mirrors the law that became effective in August 1997 that

removed the 4% minimum COLA. (Employees retiring after that date will receive annual COLAs based upon 80% of the CPI with a maximum of 5%.) However, all members who retire under the closed plan receive an annual minimum COLA of 4% until reaching the 65% cumulative cap; thereafter, the 4% percent minimum is eliminated.

It is important to note the trade-off in these plan provisions. The Year 2000 Plan was designed to specifically achieve certain policy and personnel objectives, correct benefit inequities, and to promote individual choice. The decision to extend participation in the new retirement plan to all active members, terminated-vested members and retirees was based on recognition of individual needs – in essence, allowing these groups, particularly retirees, to take advantage of the increased multiplier if their personal circumstances so warranted.

The SRAC heard testimony from retirees concerning increases in their cost of living following retirement. Retirees seek an increase in the benefit multiplier to help defer the rising costs of such things as health care and prescription drugs, and to also make this group feel as though they are being treated the same as retirees who elect to transfer to the Year 2000 Plan.

### Recommendation on HB 1847

The SRAC recognized that the Year 2000 Plan was designed to specifically achieve certain policy and personnel objectives, correct benefit inequities, promote individual choice (current retirees may elect to transfer to the Year 2000 Plan), and to accomplish all of these goals without increasing the state's costs for retirement programs. Also, the SRAC believes that providing the 1.7% formula in the closed plan would be a step backward in the pursuit of benefit equity. The SRAC pointed out that the 1.7% formula is already available to all past, present, and future employees through the new plan and to incorporate that formula in the old plan would create a benefit disparity between the new and old plans.

## RETIREE HEALTH CARE

The SRAC recognized that retirees need some relief from rapidly rising health care costs, and endorsed many of the concepts that were addressed in the Report of the House Interim Committee on Employee Health Care Contributions. The House Interim Committee's findings on this issue state that:

- Health care costs bear disproportionately on employees in lower-paying jobs.
- Most employers require retirees to bear at least some part of health care costs.
- Health care insurance costs are increasingly difficult to predict and keep stable.

Further, the House Interim Committee suggested that a health care system with desirable characteristics would:

- Be aligned with the state's existing policy on benefits.
- Reward consistent with length of service.
- Be easily understandable and not create additional levels of bureaucracy.
- Encourage equity across departments.
- Encourage equity across levels of pay (no differences exist in the quality of care available to both the highest and lowest paid employees).

The SRAC endorsed these key concepts and appointed a subcommittee to explore and recommend a structure that was consistent with the characteristics previously noted. The subcommittee worked with representatives from the Missouri Consolidated Health Care Plan (MCHCP) and evaluated several retirement health care models wherein the percentage of subsidy was based upon an employee's length of service.

As illustrated on the tables that follow, the recommended state contribution for retirees and survivors was based upon the length of state service of the respective retiree. The monthly premium cost was based on the average premium for retirees eligible for Medicare ($231); and the average premium for non-Medicare eligible ($417) retirees.

Under the proposals, each retiree would receive a subsidy toward their monthly premium of 2.5% per year of service, based upon the applicable low cost plan option, for each full year of actual state service (no transferred or purchased service would be included) with a maximum subsidy of 75%. (The state contribution for dependents of retirees and survivors is not reflected in the model, however, it is estimated to result in an additional cost of approximately $3.6 million based upon the third alternative that allocates 41% to the retiree premium.)

- Under the first alternative, the minimum subsidy payable would be 12.5% at five years of service and would fall in an approximate range of the current funding level for retiree health care.
- The second alternative would provide a minimum subsidy of 34% for up to 13 years of service and would require additional funding of approximately $.6 million.
- The third alternative would provide a minimum subsidy of 41% for up to 16 years of service and would require additional funding of approximately $1.1 million.
- The last alternative would provide a minimum subsidy of 47% for up to 18 years of service and would require additional funding of approximately $1.7 million.

In each of these instances, the cost associated with dependents is not reflected – as stated previously, that is estimated to result in an additional cost of approximately $3.6 million.

## Annual Retiree Health Care Subsidy - No Minimum

| | |
|---|---|
| Monthly Premium | 417 |
| Percent Per Year | 2.50% |
| Minimum Percent | 0.00% |

| Younger Than 65 | | Subsidy | Monthly |
|---|---|---|---|
| Service | Number | Percent | Total |
| 5 | 40 | 12.5% | 2,085 |
| 6 | 22 | 15.0% | 1,376 |
| 7 | 11 | 17.5% | 803 |
| 8 | 17 | 20.0% | 1,418 |
| 9 | 7 | 22.5% | 657 |
| 10 | 60 | 25.0% | 6,255 |
| 11 | 28 | 27.5% | 3,211 |
| 12 | 42 | 30.0% | 5,254 |
| 13 | 37 | 32.5% | 5,014 |
| 14 | 32 | 35.0% | 4,670 |
| 15 | 81 | 37.5% | 12,666 |
| 16 | 53 | 40.0% | 8,840 |
| 17 | 42 | 42.5% | 7,443 |
| 18 | 51 | 45.0% | 9,570 |
| 19 | 56 | 47.5% | 11,092 |
| 20 | 71 | 50.0% | 14,804 |
| 21 | 80 | 52.5% | 17,514 |
| 22 | 77 | 55.0% | 17,660 |
| 23 | 88 | 57.5% | 21,100 |
| 24 | 92 | 60.0% | 23,018 |
| 25 | 116 | 62.5% | 30,233 |
| 26 | 124 | 65.0% | 33,610 |
| 27 | 148 | 67.5% | 41,658 |
| 28 | 146 | 70.0% | 42,617 |
| 29 | 204 | 72.5% | 61,674 |
| 30 | 933 | 75.0% | 291,796 |
| Total | 2,658 | | 676,040 |

| | |
|---|---|
| Monthly Premium | 231 |
| Percent Per Year | 2.50% |
| Minimum Percent | 0.00% |

| 65 and Older | | Subsidy | Monthly |
|---|---|---|---|
| Service | Number | Percent | Total |
| 5 | 186 | 12.5% | 5,371 |
| 6 | 97 | 15.0% | 3,361 |
| 7 | 109 | 17.5% | 4,406 |
| 8 | 137 | 20.0% | 6,329 |
| 9 | 108 | 22.5% | 5,613 |
| 10 | 309 | 25.0% | 17,845 |
| 11 | 211 | 27.5% | 13,404 |
| 12 | 237 | 30.0% | 16,424 |
| 13 | 202 | 32.5% | 15,165 |
| 14 | 171 | 35.0% | 13,825 |
| 15 | 420 | 37.5% | 36,383 |
| 16 | 305 | 40.0% | 28,182 |
| 17 | 276 | 42.5% | 27,096 |
| 18 | 242 | 45.0% | 25,156 |
| 19 | 263 | 47.5% | 28,858 |
| 20 | 326 | 50.0% | 37,653 |
| 21 | 259 | 52.5% | 31,410 |
| 22 | 286 | 55.0% | 36,336 |
| 23 | 215 | 57.5% | 28,557 |
| 24 | 198 | 60.0% | 27,443 |
| 25 | 206 | 62.5% | 29,741 |
| 26 | 198 | 65.0% | 29,730 |
| 27 | 140 | 67.5% | 21,830 |
| 28 | 152 | 70.0% | 24,578 |
| 29 | 148 | 72.5% | 24,786 |
| 30 | 1,086 | 75.0% | 188,150 |
| Total | 6,487 | | 727,633 |

| | | Monthly | Annual |
|---|---|---|---|
| 2,658 | Younger Than 65 | 676,040 | 8,112,485 |
| 6,487 | 65 and Older | 727,633 | 8,731,592 |
| 9,145 | Total | | 16,844,077 |

## Annual Retiree Health Care Subsidy - 34% Minimum

| | |
|---|---|
| Monthly Premium | 417 |
| Percent Per Year | 2.50% |
| Minimum Percent | 34.00% |

| Younger Than 65 | | Subsidy | Monthly |
|---|---|---|---|
| Service | Number | Percent | Total |
| 5 | 40 | 34.0% | 5,671 |
| 6 | 22 | 34.0% | 3,119 |
| 7 | 11 | 34.0% | 1,560 |
| 8 | 17 | 34.0% | 2,410 |
| 9 | 7 | 34.0% | 992 |
| 10 | 60 | 34.0% | 8,507 |
| 11 | 28 | 34.0% | 3,970 |
| 12 | 42 | 34.0% | 5,955 |
| 13 | 37 | 34.0% | 5,246 |
| 14 | 32 | 35.0% | 4,670 |
| 15 | 81 | 37.5% | 12,666 |
| 16 | 53 | 40.0% | 8,840 |
| 17 | 42 | 42.5% | 7,443 |
| 18 | 51 | 45.0% | 9,570 |
| 19 | 56 | 47.5% | 11,092 |
| 20 | 71 | 50.0% | 14,804 |
| 21 | 80 | 52.5% | 17,514 |
| 22 | 77 | 55.0% | 17,660 |
| 23 | 88 | 57.5% | 21,100 |
| 24 | 92 | 60.0% | 23,018 |
| 25 | 116 | 62.5% | 30,233 |
| 26 | 124 | 65.0% | 33,610 |
| 27 | 148 | 67.5% | 41,658 |
| 28 | 146 | 70.0% | 42,617 |
| 29 | 204 | 72.5% | 61,674 |
| 30 | 933 | 75.0% | 291,796 |
| Total | 2,658 | | 687,397 |

| | |
|---|---|
| Monthly Premium | 231 |
| Percent Per Year | 2.50% |
| Minimum Percent | 34.00% |

| 65 and Older | | Subsidy | Monthly |
|---|---|---|---|
| Service | Number | Percent | Total |
| 5 | 186 | 34.0% | 14,608 |
| 6 | 97 | 34.0% | 7,618 |
| 7 | 109 | 34.0% | 8,561 |
| 8 | 137 | 34.0% | 10,760 |
| 9 | 108 | 34.0% | 8,482 |
| 10 | 309 | 34.0% | 24,269 |
| 11 | 211 | 34.0% | 16,572 |
| 12 | 237 | 34.0% | 18,614 |
| 13 | 202 | 34.0% | 15,865 |
| 14 | 171 | 35.0% | 13,825 |
| 15 | 420 | 37.5% | 36,383 |
| 16 | 305 | 40.0% | 28,182 |
| 17 | 276 | 42.5% | 27,096 |
| 18 | 242 | 45.0% | 25,156 |
| 19 | 263 | 47.5% | 28,858 |
| 20 | 326 | 50.0% | 37,653 |
| 21 | 259 | 52.5% | 31,410 |
| 22 | 286 | 55.0% | 36,336 |
| 23 | 215 | 57.5% | 28,557 |
| 24 | 198 | 60.0% | 27,443 |
| 25 | 206 | 62.5% | 29,741 |
| 26 | 198 | 65.0% | 29,730 |
| 27 | 140 | 67.5% | 21,830 |
| 28 | 152 | 70.0% | 24,578 |
| 29 | 148 | 72.5% | 24,786 |
| 30 | 1,086 | 75.0% | 188,150 |
| Total | 6,487 | | 765,064 |

| | | Monthly | Annual |
|---|---|---|---|
| 2,658 | Younger Than 65 | 687,397 | 8,248,769 |
| 6,487 | 65 and Older | 765,064 | 9,180,767 |
| 9,145 | Total | | 17,429,536 |

## Annual Retiree Health Care Subsidy - 41% Minimum

| | |
|---|---|
| Monthly Premium | 417 |
| Percent Per Year | 2.50% |
| Minimum Percent | 41.00% |

| Younger Than 65 | | Subsidy | Monthly |
|---|---|---|---|
| Service | Number | Percent | Total |
| 5 | 40 | 41.0% | 6,839 |
| 6 | 22 | 41.0% | 3,761 |
| 7 | 11 | 41.0% | 1,881 |
| 8 | 17 | 41.0% | 2,906 |
| 9 | 7 | 41.0% | 1,197 |
| 10 | 60 | 41.0% | 10,258 |
| 11 | 28 | 41.0% | 4,787 |
| 12 | 42 | 41.0% | 7,181 |
| 13 | 37 | 41.0% | 6,326 |
| 14 | 32 | 41.0% | 5,471 |
| 15 | 81 | 41.0% | 13,849 |
| 16 | 53 | 41.0% | 9,061 |
| 17 | 42 | 42.5% | 7,443 |
| 18 | 51 | 45.0% | 9,570 |
| 19 | 56 | 47.5% | 11,092 |
| 20 | 71 | 50.0% | 14,804 |
| 21 | 80 | 52.5% | 17,514 |
| 22 | 77 | 55.0% | 17,660 |
| 23 | 88 | 57.5% | 21,100 |
| 24 | 92 | 60.0% | 23,018 |
| 25 | 116 | 62.5% | 30,233 |
| 26 | 124 | 65.0% | 33,610 |
| 27 | 148 | 67.5% | 41,658 |
| 28 | 146 | 70.0% | 42,617 |
| 29 | 204 | 72.5% | 61,674 |
| 30 | 933 | 75.0% | 291,796 |
| Total | 2,658 | | 697,307 |

| | |
|---|---|
| Monthly Premium | 231 |
| Percent Per Year | 2.50% |
| Minimum Percent | 41.00% |

| 65 and Older | | Subsidy | Monthly |
|---|---|---|---|
| Service | Number | Percent | Total |
| 5 | 186 | 41.0% | 17,616 |
| 6 | 97 | 41.0% | 9,187 |
| 7 | 109 | 41.0% | 10,323 |
| 8 | 137 | 41.0% | 12,975 |
| 9 | 108 | 41.0% | 10,229 |
| 10 | 309 | 41.0% | 29,265 |
| 11 | 211 | 41.0% | 19,984 |
| 12 | 237 | 41.0% | 22,446 |
| 13 | 202 | 41.0% | 19,131 |
| 14 | 171 | 41.0% | 16,195 |
| 15 | 420 | 41.0% | 39,778 |
| 16 | 305 | 41.0% | 28,887 |
| 17 | 276 | 42.5% | 27,096 |
| 18 | 242 | 45.0% | 25,156 |
| 19 | 263 | 47.5% | 28,858 |
| 20 | 326 | 50.0% | 37,653 |
| 21 | 259 | 52.5% | 31,410 |
| 22 | 286 | 55.0% | 36,336 |
| 23 | 215 | 57.5% | 28,557 |
| 24 | 198 | 60.0% | 27,443 |
| 25 | 206 | 62.5% | 29,741 |
| 26 | 198 | 65.0% | 29,730 |
| 27 | 140 | 67.5% | 21,830 |
| 28 | 152 | 70.0% | 24,578 |
| 29 | 148 | 72.5% | 24,786 |
| 30 | 1,086 | 75.0% | 188,150 |
| Total | 6,487 | | 797,342 |

| | | Monthly | Annual |
|---|---|---|---|
| 2,658 | Younger Than 65 | 697,307 | 8,367,689 |
| 6,487 | 65 and Older | 797,342 | 9,568,099 |
| 9,145 | Total | | 17,935,787 |

# Annual Retiree Health Care Subsidy - 47% Minimum

| | |
|---|---|
| Monthly Premium | 417 |
| Percent Per Year | 2.50% |
| Minimum Percent | 47.00% |

| Younger Than 65 | | Subsidy | Monthly |
|---|---|---|---|
| Service | Number | Percent | Total |
| 5 | 40 | 47.0% | 7,840 |
| 6 | 22 | 47.0% | 4,312 |
| 7 | 11 | 47.0% | 2,156 |
| 8 | 17 | 47.0% | 3,332 |
| 9 | 7 | 47.0% | 1,372 |
| 10 | 60 | 47.0% | 11,759 |
| 11 | 28 | 47.0% | 5,488 |
| 12 | 42 | 47.0% | 8,232 |
| 13 | 37 | 47.0% | 7,252 |
| 14 | 32 | 47.0% | 6,272 |
| 15 | 81 | 47.0% | 15,875 |
| 16 | 53 | 47.0% | 10,387 |
| 17 | 42 | 47.0% | 8,232 |
| 18 | 51 | 47.0% | 9,995 |
| 19 | 56 | 47.5% | 11,092 |
| 20 | 71 | 50.0% | 14,804 |
| 21 | 80 | 52.5% | 17,514 |
| 22 | 77 | 55.0% | 17,660 |
| 23 | 88 | 57.5% | 21,100 |
| 24 | 92 | 60.0% | 23,018 |
| 25 | 116 | 62.5% | 30,233 |
| 26 | 124 | 65.0% | 33,610 |
| 27 | 148 | 67.5% | 41,658 |
| 28 | 146 | 70.0% | 42,617 |
| 29 | 204 | 72.5% | 61,674 |
| 30 | 933 | 75.0% | 291,796 |
| Total | 2,658 | | 709,279 |

| | |
|---|---|
| Monthly Premium | 231 |
| Percent Per Year | 2.50% |
| Minimum Percent | 47.00% |

| 65 and Older | | Subsidy | Monthly |
|---|---|---|---|
| Service | Number | Percent | Total |
| 5 | 186 | 47.0% | 20,194 |
| 6 | 97 | 47.0% | 10,531 |
| 7 | 109 | 47.0% | 11,834 |
| 8 | 137 | 47.0% | 14,874 |
| 9 | 108 | 47.0% | 11,726 |
| 10 | 309 | 47.0% | 33,548 |
| 11 | 211 | 47.0% | 22,908 |
| 12 | 237 | 47.0% | 25,731 |
| 13 | 202 | 47.0% | 21,931 |
| 14 | 171 | 47.0% | 18,565 |
| 15 | 420 | 47.0% | 45,599 |
| 16 | 305 | 47.0% | 33,114 |
| 17 | 276 | 47.0% | 29,965 |
| 18 | 242 | 47.0% | 26,274 |
| 19 | 263 | 47.5% | 28,858 |
| 20 | 326 | 50.0% | 37,653 |
| 21 | 259 | 52.5% | 31,410 |
| 22 | 286 | 55.0% | 36,336 |
| 23 | 215 | 57.5% | 28,557 |
| 24 | 198 | 60.0% | 27,443 |
| 25 | 206 | 62.5% | 29,741 |
| 26 | 198 | 65.0% | 29,730 |
| 27 | 140 | 67.5% | 21,830 |
| 28 | 152 | 70.0% | 24,578 |
| 29 | 148 | 72.5% | 24,786 |
| 30 | 1,086 | 75.0% | 188,150 |
| Total | 6,487 | | 835,868 |

| | | Monthly | Annual |
|---|---|---|---|
| 2,658 | Younger Than 65 | 709,279 | 8,511,354 |
| 6,487 | 65 and Older | 835,868 | 10,030,413 |
| 9,145 | Total | | 18,541,766 |

## Findings and Conclusions on Retiree Health Care

After reviewing the various proposals, the SRAC determined that the most desirable retiree health care model would provide:

- A subsidy toward a retiree's monthly premium of 2.5% per year of service based upon the applicable low cost plan option for each full year of actual state service with a maximum subsidy of 75%.

- A subsidy to current and future retirees that would be the greater of a service based formula or a minimum dollar amount based on the current state subsidy. (The rationale behind such a minimum would be to prevent an exodus of active employees who might seek to immediately leave the workforce in order to take advantage of a more highly subsidized health care premium and to not penalize current retirees who have accrued less service.)

- A subsidy toward retiree dependent coverage targeted at 75% of the active subsidy percentage and floored at the current dollar amount.

- No state subsidy for terminated-vested members who have discontinued their MCHCP coverage but who elect to again be covered by MCHCP at the time of retirement.

## Recommendation on Retiree Health Care

Given the current volatile nature of the health care industry, the SRAC believes a service-based health care model will serve as a future cost containment measure and will also ensure that the same quality of care is available to both the highest and lowest paid employees. The SRAC recommends adoption of the model that provides a subsidy towards a retiree's monthly premium of 2.5% per year of service based upon the applicable low cost plan option for each full year of actual state service with a maximum subsidy of 75% and the minimum subsidies stated above.

The SRAC further recommends that implementation should begin as soon as the MCHCP Board of Trustees approves the plan, but no later than the next plan year. It is anticipated that MCHCP should seek statutory authority for the service-based subsidy method, however, the detail could be defined through MCHCP's rule and regulations. Additional funding for this plan, if needed, would be subject to appropriations authorized by the General Assembly. The SRAC recommends that MCHCP's staff work closely with the appropriations committees prior to implementation. If the minimum subsidy model is adopted and funding for the level recommended is not appropriated, the subsidy should be reduced proportionally.

It should be that noted that the SRAC did not have unanimous support for this recommendation. Concerns were raised regarding the minimum subsidy and the possibility that appropriations would not be available to cover the additional expense combined with the expectations that retirees might develop regarding a "guaranteed" subsidy. The Department of Conservation also expressed its opposition based on concerns that such a model could not be cost-neutral to their plan because their present retiree subsidy is approximately 34% of the premium expense. (The Department of Conservation provides its own insurance coverage for its employees.) It was also noted that the average Department of Conservation retiree terminates employment at 30 years of service – thus increased costs would be anticipated under the service-based model. Further, the Department of Conservation has concerns regarding substantially reducing the subsidy available for new hires in order to offset an increased subsidy for present long-service retirees. Lastly, the Department of

Conservation has expressed concerns regarding their department making available two-tiered levels of benefits as it relates to retiree health care.

MoDOT (which includes the Highway Patrol) currently administers its own health care program and offers a retiree health care subsidy equivalent to 34% of the expense. The SRAC recommends that this department consult with the MCHCP to determine whether or not adoption of the proposed retiree health care model is feasible for their department.

## New Developments

After the SRAC completed its meetings, the Administration and the Missouri Consolidated Health Care Plan took action to increase the health insurance subsidy for retirees for calendar year 2001. As stated previously, the SRAC recommended a minimum subsidy that was based on 41% of the low cost plan. As a result of this recent activity, the state subsidy for retiree health care for next year will be in the range of 54%-60%. The SRAC believes that this action could exert upward pressure on the state to increase the recommended minimum subsidy in the proposed service-based model.

The SRAC was also informed that the MOSERS' Board of Trustees is exploring the concept of pre-funding a portion of the state subsidy for retiree health care. (Such action would require that MOSERS be granted legislative authority in this area before pre-funding could commence.)

In light of these new developments, the SRAC recommends that the TFTC work closely with the MCHCP to further investigate the impact of the recent increased subsidy for retiree health care and how that increase might affect the recommended service-based model.

# PENSION TAX EXEMPTION LEGISLATION

## House Bill 1159 (HB 1159)

During the last session of the General Assembly, 11 various tax exemption proposals were introduced. One of these proposals, HB 1159, sponsored by Representative Bill Boucher, moved through both houses of the General Assembly, however, was not truly agreed to and finally passed. This particular proposal would have eliminated the phase-in and exempted all retirement income from taxation beginning with tax year 2002. The estimated loss to general revenue was $148.4 million in fiscal year 2002 and $202.7 million in fiscal year 2003. It is anticipated that this proposal will be filed again in the upcoming session.

## Recommendation on HB 1159

The SRAC heard testimony from retirees, and other groups interested in obtaining additional tax relief to ease the financial burden associated with rising costs in retirement. The SRAC was unable to adequately explore and make a recommendation on this issue due to time constraints and the number of other complex legislative retirement proposals that the SRAC was charged with evaluating. More importantly, the SRAC felt that the issue of pension tax exemption legislation extended beyond the scope of their charge and should be evaluated by those with expertise in the taxation/revenue area.

# DEFERRED COMPENSATION LEGISLATION

## Senate Bill 1022 (SB 1022)

Legislation sponsored by Senator John Scott last session, SB 1022, would have transferred oversight of the Deferred Compensation Program from the Missouri State Employees' Deferred Compensation Commission to the Board of Trustees of MOSERS.

Members from the subcommittees of the Deferred Compensation Commission and the MOSERS' Board of Trustees reported to the SRAC that they have met jointly to discuss their plans' structures, responsibilities, interests, and alternatives for the future. These groups are working on recommendations pertaining to:

- The design and characteristics of a coordinated optimum retirement benefit structure for state employees, taking into consideration the benefits provided by the state's defined benefit plan and the deferred compensation plan, as well as the administrative and managerial issues common to both.
- Analysis of how the current retirement benefit structure differs from the optimum structure.
- Recommendations for moving from the current structure toward the optimum retirement benefit structure.

## Recommendation on SB 1022

The SRAC is supportive of measures that provide better coordination of benefits and communications that work in the best interest of the plan participants. The SRAC recommends that the two boards continue to work towards achieving improved service delivery and a better understanding by state employees of the overall benefit package.

# OTHER RECOMMENDATIONS

The SRAC noted that the TFTC has proven to be an effective means of ensuring that the state, as an employer, utilizes a comprehensive approach in assessing the appropriateness of salary and benefit levels for state employees. Although the TFTC will terminate its operations at the end of the year, the SRAC recommends that a similar board or commission be established through enabling legislation. This new board or commission would be given the task of evaluating policy and recommended courses of action relating to total compensation, retirement, health care, and other benefits for state employees under the Executive Branch on a permanent basis.

MOSERS

Gary W. Findlay
Executive Director

Missouri State Employees' Retirement System

TO: SRAC Members

FROM: Gary Findlay

SUBJECT: Public Pension Portability in the State of Missouri

DATE: July 21, 2000

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In light of our discussions regarding ORP, it occurred to me that you might find it useful to have an overview of other public pension portability provisions that presently exist within the state.

### *Portability Defined*

For purposes of this overview, the term "portability" describes retirement plan provisions that allow an individual employee to move from one employer to the next without any significant impairment of the pension benefits that are being accrued.

### *What Portability Provisions Exist Today In Missouri Within Systems?*

#### MOSERS

General employees may move among state agencies covered by MOSERS without negatively impacting their retirement benefits. A common benefit formula and single final average salary period are used in computing benefits.

Members of the general assembly have certain options available for transferring service between the general assembly plan and the general employee or statewide elected official plans.

Except as otherwise provided by law, up to five years of service may be transferred to or from any of the following: general employee plan, general assembly plan, statewide elected official plan, judicial plan, and administrative law judge plan. Any service remaining in the transferring plan after the transfer is forfeited.

#### HTEHPRS

Employees may move among MoDOT and certain positions in the Department of Public Safety covered by HTEHPRS without negatively impacting their retirement benefits. A common benefit formula and single final average salary period are used in computing benefits.

#### LAGERS

Local government employees may move from one LAGERS' covered employer to the next without negatively impacting their retirement benefit accruals. This is because when the employee finally retires, the benefit amount attributable to each period of employment with different employers will be based on the final average salary period producing the highest average. For example, if an employee works for 15

years for Joplin and then works another 15 years for Springfield and then retires, the benefit charged to Joplin would be based on the benefit plan in effect at Joplin when the employee left service there but on the final average salary earned at Springfield. In other words, in this case a portion of Joplin's liability for this individual is predicated on pay raises received while at Springfield. (The employee's benefit and the cost to Joplin would have been significantly less if the benefit for service at Joplin had been predicated on the pay history with Joplin.)

**PSRS**

In the Public School Retirement System, employees may move from one school district to the next without impairing their retirement benefits (except for moves between PRSR and the Kansas City and St. Louis districts). In the case of moves within the PSRS family of districts, all employers have the same contribution rate and the same benefit formula. Just as within LAGERS, a common final average salary is used regardless of the number of different employers involved. In evaluating the contribution rate required to support their benefits, the actuary gives recognition to the fact that this type of portability exists.

**NTRS**

In the Non-Teachers Retirement System, employees may move from one school district to the next without impairing their retirement benefits (except for moves between NTRS and the Kansas City and St. Louis districts). In the case of moves within the NTRS family of districts, all employers have the same contribution rate and the same benefit formula. Just as within LAGERS, a common final average salary is used regardless of the number of different employers involved. In evaluating the contribution rate required to support their benefits, the actuary gives recognition to the fact that this type of portability exists.

**CERF**

In the County Employees' Retirement Fund, a common final average salary is used regardless of the number of counties in which the individual was employed. Effectively, this is the same as the LAGERS approach to within system portability.

## *What Portability Provisions Exist Today In Missouri Among The Different Systems?*

**ALL SYSTEMS**

In 1992, Section 105.691 of the Revised Statutes of Missouri became law. This provision allows for very limited portability of service among systems. Under the definition of portability stated earlier (calling for no or only limited impairment of retirement benefits in connection with changing employers), this provision does not really provide for portability at all.

One example of the way it works is as follows: If a terminated vested member of LAGERS becomes a state employee and becomes vested in MOSERS, that employee may request LAGERS to transfer to MOSERS an amount equal to the liability LAGERS has on the books for that person. MOSERS would, in turn, compute how much service credit the individual could receive in connection with the amount transferred from LAGERS. The dollar amount transferred from LAGERS was computed on the basis of the salary history of the person upon leaving LAGERS covered employment. The liability for an equal

amount of service under MOSERS would be computed on the basis of salary projected out to expected retirement. Because of the treatment of salary for purposes of these calculations, it is not unusual for the liability of the receiving system to be about ten times larger than the liability from the transferring system. If the 10 to 1 ratio applied in a particular case, an employee who had ten years of LAGERS service credit could receive one year of service credit under MOSERS and could then buy the other nine years at the full actuarial cost. (The same would be true if the transfer were from MOSERS to LAGERS.)

As you can imagine, transfers under this provision are rare (generally in connection with someone attempting to get additional service credit to establish retirement eligibility under a "rule of 80" provision).

## BETWEEN MOSERS AND HTEHPRS

Employees with service credit in both systems may combine the service into the system in which the employee is currently receiving service without negatively impacting their retirement benefits. A common benefit formula and single final average salary period are used in computing benefits.

Except as otherwise provided by law, up to five years of service may be transferred to or from HTEHPRS and any of the following: general employee plan, general assembly plan, statewide elected official plan, judicial plan, and administrative law judge plan. Any service remaining in the transferring plan after the transfer is forfeited.

## BETWEEN MOSERS AND PACARS

Up to five years of service may be transferred to or from the Prosecutors' and Circuit Attorneys' Retirement System and any of the following: general employee plan, general assembly plan, statewide elected official plan, judicial plan, and administrative law judge plan. Any service remaining in the transferring plan after the transfer is forfeited.

## TO MOSERS OR HTEHPRS FROM ALL OTHER SYSTEMS

Under the provisions of Section 104.1090 which became effective July 1, 2000, employees who have at least ten years of MOSERS or HTEHPRS service credit may have service credit which is vested in another public retirement system in Missouri transferred to the state system under the condition that the previous system will transfer to the state system an amount equal to the liability the transferring system has for that individual. (If the transferring system is not fully funded, the amount transferred to the state system will be equal to the liability times the percent funded.) In exchange for the transfer, the employee will receive 1 to 1 service credit under the state system.

### *Conclusion*

I hope this summary serves as a useful tool as we discuss further the issue of portability at our next meeting. If you have any questions in the meantime, please call.

EXECUTIVE ORDER
NO. 00-11

WHEREAS, it is in the best interests of the State of Missouri, as an employer, to monitor legislative proposals relating to retirement and other employee benefits for state employees; and

WHEREAS, changes to the State of Missouri's retirement plans have evolved in a rather fragmented fashion over the past several decades necessitating a more comprehensive approach for evaluating employee benefits; and

WHEREAS, the State of Missouri and the retirement systems have been named as defendants in a number of lawsuits that claimed that certain retirement statutes have created inequities resulting in violations of the equal protection provisions of the state and federal constitutions which have resulted in both the state and the retirement systems incurring significant liabilities; and

WHEREAS, the State of Missouri, as an employer, has adopted personnel management objectives targeted at allowing the state to recruit, retain and pay employees who provide the highest quality services to the citizens of the state through a benefits structure, combined with appropriate pay, that is designed to provide financial security to state employees in an equitable and cost-effective manner; and

WHEREAS, through the enactment of the Year 2000 Retirement Plan, the State of Missouri through the General Assembly, has addressed inequities in the retirement laws covering state employees and adopted the following specific policy goals of:

a) reducing turnover among younger employees;
b) encouraging retirement before social security eligibility to provide opportunities for promotion for younger employees;
c) reducing payroll costs;
d) refreshing the workforce;
e) addressing hazardous position needs;
f) providing for all dependents in the event of duty related death;
g) facilitating local to state employment mobility for recruitment purposes; and

WHEREAS, the Governor has established the Ad Hoc Task Force on Total Compensation for the purpose of evaluating and recommending courses of action related to total compensation, including retirement and other benefits, to ensure that a comprehensive approach is utilized in assessing the appropriateness of salary and benefit levels for state employees; and

WHEREAS, the Ad Hoc Task Force on Total Compensation is interested in receiving input from qualified professionals who have expertise in the areas of retirement to provide guidance and recommendations on legislative proposals introduced during the second regular session of the 90th General Assembly that will modify the structure of and benefits provided by the state retirement plans; and

WHEREAS, the Missouri State Employees' Retirement System and the Highway and Transportation Employees' and Highway Patrol Retirement System currently administer separate retirement programs for state employees;

NOW, THEREFORE, I, Mel Carnahan, Governor of the State of Missouri, by virtue of the authority vested in me by the Constitution and laws of the State of Missouri, do hereby establish the State Retirement Advisory Commission whose task will be to analyze proposals regarding retirement benefits for state employees to ensure that they are consistent with the policy goals and personnel management objectives set forth above. The commission shall be composed of the following:

- one member of the Ad Hoc Task Force on Total Compensation who shall be appointed by the Chairman of the Task Force;

- one member of the Board of Trustees of the Missouri State Employees' Retirement System to be appointed by the Chairman of the Board of Trustees;

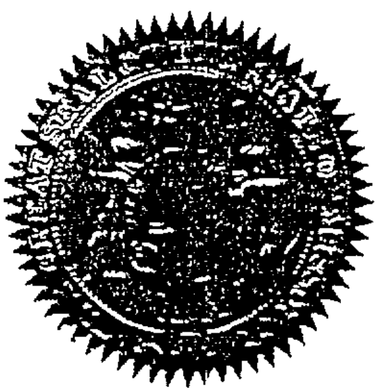
- one member of the Board of Trustees of the Highway and Transportation Employees' and Highway Patrol Retirement System to be appointed by the Chairman of the Board of Trustees;

- the Chairman and Executive Director of the Missouri General Assembly's Joint Committee on Public Employee Retirement and another member of the Committee appointed by the Chairman;
- the Executive Directors of the Missouri State Employees' Retirement System and the Highway and Transportation Employees' and Highway Patrol Retirement System;
- the Commissioner of Administration or an appointed designee;
- the Director of the Department of Public Safety;
- the Commissioner of Higher Education; and
- an Administrative Hearing Commissioner appointed by the Governor.

The State Retirement Advisory Commission will coordinate and meet with representatives of state departments, boards and commissions and the General Assembly on retirement issues that affect employees in their respective areas of responsibility.

The State Retirement Advisory Commission shall commence immediately and shall terminate operations on December 31, 2000. The State Retirement Advisory Commission shall furnish to the Ad Hoc Task Force on Total Compensation clear policy recommendations on legislative proposals considered in the second regular session of the 90th General Assembly, and other recommendations pertaining to retirement as deemed necessary, in a final report to be issued no later than September 30, 2000. A copy of the report shall be submitted to the Governor by the Ad Hoc Task Force on Total Compensation no later than November 30, 2000, and shall include a separate addendum containing the Task Force's recommended course of action.

The State Retirement Advisory Commission shall, upon request, receive assistance and cooperation from the various departments of state government which have a stake in the outcome of the State Retirement Advisory Commission's activity.



IN WITNESS WHEREOF, I have hereunto set my hand and caused to be affixed the Great Seal of the State of Missouri, in the City of Jefferson, on this 28th day of April, 2000.

GOVERNOR

SECRETARY OF STATE

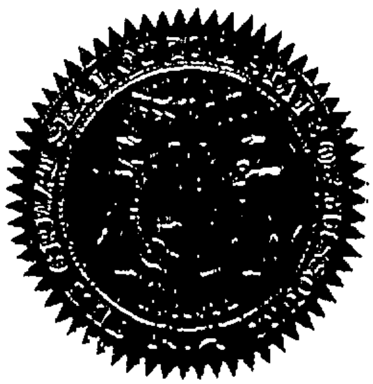
EXECUTIVE ORDER
00-14

WHEREAS, Executive Order No. 00-11 was issued April 28, 2000, establishing the State Retirement Advisory Commission; and

WHEREAS, the name of the chairperson was omitted ; and

WHEREAS, the Governor has appointed Commissioner Karen Winn of the Administrative Hearing Commission.

NOW, THEREFORE, I, Mel Carnahan, Governor of the State of Missouri, by virtue of the authority vested in me by the Constitution and laws of the State of Missouri, do hereby name Karen Winn Chairperson of the State Retirement Advisory Commission.



In WITNESS WHEREOF, I have hereunto set my hand and caused to be affixed the Great Seal of the State of Missouri, in the City of Jefferson, on this 22nd day of June, 2000.

GOVERNOR

ATTEST:

SECRETARY OF STATE

Governor Mel Carnahan

# AD HOC TASK FORCE ON TOTAL COMPENSATION

Chairperson Jerry Conley

November 30, 2000

The Honorable Roger Wilson
Governor of Missouri
Capitol Building, Room 216
Jefferson City, Missouri 65101

Dear Governor Wilson:

On behalf of the Ad Hoc Task Force on Total Compensation (TFTC) and the State Retirement Advisory Commission (SRAC), I am pleased to present our findings and recommendations as required by Executive Order 00-11. The SRAC provided the TFTC with a detailed report and recommendations pertaining to retirement legislation introduced during the last legislative session, as well as other recommendations pertaining to specific issues experienced by retirees in retirement.

The TFTC reviewed the report and considered the proposed recommendations. Members of the TFTC voted to endorse the recommendations contained in the SRAC report with the exception of legislation that would create a separate retirement plan for the regional colleges and universities. This issue is discussed on page one of the Addendum, and on page 21 of the SRAC report.

We sincerely hope that you and the General Assembly will find these recommendations useful in our collective efforts to provide state employees with financial security in an equitable and cost-effective manner.

Sincerely,

JERRY M. CONLEY, Chair
Ad Hoc Task Force on Total Compensation

Enclosures

c: Members
Resource Staff

# AD HOC TASK FORCE ON TOTAL COMPENSATION

# ADDENDUM TO STATE RETIREMENT ADVISORY COMMISSION REPORT

Executive Order 00-11 requires the Ad Hoc Task Force on Total Compensation (TFTC) to issue an addendum to the State Retirement Advisory Commission (SRAC) report by November 30, 2000. The SRAC report contains recommendations on a number of legislative proposals considered in the second regular session of the 90th General Assembly. This addendum contains a recommended course of action regarding each of the SRAC recommendations.

## *WORKFORCE SHORTAGE*

### *HB 2069 – DROP legislation*

SRAC recommendation: A Deferred Retirement Option Plan (DROP) is an optional payment form under a defined benefit plan that allows members to receive a partial lump sum payment of his/her retirement account in addition to a reduced monthly life retirement benefit. The SRAC determined that valuable, long-service employees could possibly be induced to delay their retirement if a DROP was added to the current menu of retirement options. Adding this payment option to the retirement systems could afford state agencies the opportunity to further enhance their succession planning efforts, and ease the transition problems associated with retirement. If the TFTC is supportive of this conclusion, the SRAC recommends that legislation be drafted and introduced that would make the proposed back DROP model available to members retiring under Chapter 104 RSMo (other than elected officials and members of the general assembly).

*TFTC recommendation:* The TFTC concurs with this recommendation. The DROP legislation should be cost neutral, should be available to all similarly situated employees, and should be designed to prevent employees from making poor choices.

## *RECIPROCITY, PORTABILITY, AND PUBLIC EMPLOYEE PLANS*

### *HB 1660 – ORP legislation*

*SRAC recommendation:* In the past decade, legislation has been introduced nearly every year which would have allowed each of the regional colleges and universities to establish an Optional Retirement Plan (ORP) for all full-time faculty and senior administrative personnel. Under these proposals, all future employees of the institutions in these classifications would have been allowed to elect participation in an ORP in lieu of

participating in MOSERS. In some versions of the legislation, participation also would have been extended to current members of MOSERS who were employed in ORP eligible positions at these institutions.

The fundamental question facing the state is whether or not it should deviate from the "attract and retain" philosophy embedded in the existing retirement plan and, as a consequence, facilitate employee movement to other employers. Although the colleges and universities maintain that that the current defined benefit plan's lack of portability discourages some job candidates from taking positions with Missouri colleges, that can also be said for the recruitment of certain positions at all state agencies. After much discussion, the SRAC determined that establishing an ORP for the regional colleges and universities would run counter to the "attract and retain" philosophy that has been promoted by the state and endorsed in the Year 2000 Plan.

*If it is determined that faculty and senior administrative personnel of the colleges and universities truly have different needs than other state agencies*, then the SRAC would recommend an alternative to the ORP model proposed in the past. *The University Retirement Plan (URP)* alternative model would establish a defined contribution plan with immediate vesting for faculty and senior administrative personnel at the regional colleges and universities who are hired after the effective date of the legislation. There would be no option – all qualifying personnel would automatically participate in the defined contribution plan. (Since it is not needed to attract employees who are already there, it should not be extended to the present population.)

*TFTC recommendation:* The TFTC opposes this recommendation. Although the URP approach would address most of the problematic design issues associated with past ORP proposals – specifically, equal protection, adverse selection, and irrevocable elections – the TFTC believes creating a separate retirement plan for certain groups is detrimental to the defined benefit plan. The defined benefit plan structure is designed to meet key human resource objectives, particularly reducing turnover among younger employees (with a career goal of 30 years of service.) A defined contribution plan structure runs counter to this objective by facilitating turnover among younger employees with less service. In addition, the creation of special provisions for a select group of employees (particularly for highly compensated employees) creates the perception of unfairness or inequity among rank and file state employees. Benefit equity among employees in all state agencies is compromised with the establishment of a separate retirement plan for faculty and administrative personnel at the state colleges and universities.

## *BENEFIT EQUITY*

### *SB 863 and HB 1914; HB 16645 and SB 813 – Public Safety legislation*

*SRAC recommendation:* SB 863 and HB 1914 would have provided uniformed conservation agents (both active and terminated-vested employees), retirees, and survivors with an additional 33.3% retirement benefit in the Missouri State Employees'

***TFTC recommendation:*** The TFTC concurs with the concept of basing the state's contribution for retiree health care upon the individual's length of service. The TFTC further endorses a minimum subsidy floor and maximum ceiling to be established for current retirees and that the state's contribution rate for retiree dependent coverage would not exceed the state's contribution for dependents of active employees. For current retirees, the proposal should provide that the current dollar amounts of the state's contribution would remain the same. New retirees would utilize the longevity based rate structure. The TFTC encourages a phased-in implementation of this model as soon as possible. The details of this approach would have to be finalized in consultation with staff from MCHCP, Governor's Office and the Legislature and other affected groups.

The actual numbers may vary based on the formula selected; however the philosophy of a service based approach has been endorsed and encouraged.

*House Bill 1159 – Pension Tax Exemption legislation*

***SRAC recommendation:*** During the last session of the General Assembly, 11 various pension income tax exemption proposals were introduced. One of these proposals, HB 1159 (Boucher) moved through both houses of the General Assembly, however, was not truly agreed to and finally passed. This particular proposal would have eliminated the phase-in and exempted all retirement income from taxation beginning with tax year 2002. The estimated loss to general revenue was $148.4 million in fiscal year 2002 and $202.7 million in fiscal year 2003. It is anticipated that this proposal will be filed again in the upcoming session.

The SRAC heard testimony from retirees, and other groups interested in obtaining additional tax relief to ease the financial burden associated with rising costs in retirement. The SRAC was unable to adequately explore and make a recommendation on this issue due to time constraints and the number of other complex legislative retirement proposals that the SRAC was charged with evaluating. ***More importantly, the SRAC felt that the issue of pension income tax exemption legislation extended beyond the scope of their charge and should be evaluated by those with expertise in the taxation/revenue area.***

***TFTC recommendation:*** The TFTC concurs with this recommendation.

*Senate Bill 1022 – Deferred Compensation legislation*

***SRAC recommendation:*** SB 1022 (Scott) would have transferred oversight of the Deferred Compensation Program from the Missouri State Employees' Deferred Compensation Commission to the Board of Trustees of MOSERS. Members from the subcommittees of the Deferred Compensation Commission and the MOSERS' Board of Trustees reported to the SRAC that they have met jointly to discuss their plans' structures, responsibilities, interests, and alternatives for the future.

The SRAC is supportive of measures that provide better coordination of benefits and communications that work in the best interest of the plan participants. The SRAC recommends that the two boards continue to work towards achieving improved service delivery and a better understanding by state employees of the overall benefit package.

***TFTC recommendation:*** The TFTC concurs with this recommendation.

*Total Compensation Board or Commission*

***SRAC recommendation:*** The SRAC noted that the TFTC has proven to be an effective means of ensuring that the state, as an employer, utilizes a comprehensive approach in assessing the appropriateness of salary and benefit levels for state employees. Although the TFTC terminates operations on December 31, 2000, the SRAC recommends that a similar board or commission be established through enabling legislation. This new board or commission would be given the task of evaluating policy and recommended actions relating to total compensation, retirement, health care, and other benefits for state employees under the Executive Branch on a permanent basis.

***TFTC recommendation:*** The TFTC concurs with this recommendation. The advisory function of the TFTC has provided the administration and legislators with additional information when considering salary and benefits proposals. Proposals can be measured against specific state human resource objectives and scarce resources can be directed toward the most equitable, comprehensive and appropriate proposals.

Plan (MSEP). HB 1665 and SB 813 would have provided a burial benefit and a lump sum death benefit to certain local and state government public safety officers killed in the line of duty. Only specific classifications of state employees named in the legislation would have been eligible to receive these benefits.

The SRAC believes that the issues associated with offering separate benefits for public safety employees were sufficiently and thoroughly explored by the Public Safety Retirement Advisory Commission (PSRAC) in 1998, and resolved through the enactment of the Year 2000 Plan (or MSEP 2000). The MSEP 2000 does not provide different benefit levels for general employees and public safety type classifications. Further, the SRAC believes that the state has adequately addressed the issues of employer responsibility for duty-related death by providing a 50% percent of final average pay minimum death benefit and expanding the state's basic life insurance coverage to include triple indemnity provisions and increased basic coverage amounts. Because these issues have been addressed for all state employees, the SRAC voted to oppose the additional one-third retirement benefit for conservation agents and special death and burial benefits for state public safety employees.

***TFTC recommendation:*** The TFTC concurs. The Year 2000 Plan is designed to provide equitable benefits to all state employees, regardless of their classification. The state could be exposed to additional equal protection lawsuits from other employee groups if enhanced benefits are provided to certain classifications of public safety employees.

*HB 2090 Public Service Commission legislation*

***SRAC recommendation:*** This legislation would have transferred regulatory law judges appointed by the Public Service Commission from MOSERS' General Employee Plan to the Administrative Law Judges' and Legal Advisors' Plan (ALJLAP). The PSC indicated that turnover due to low salaries is a significant problem for the agency. While the PSC is attempting to address the pay issue through appropriations, they believe expanding membership in the ALJLAP (which has a significantly higher benefit formula than the general employee plan) to include regulatory law judges would help resolve their retention issue.

The SRAC was unable to adequately explore and resolve this issue due to time constraints. The SRAC recommends that a separate commission be appointed to further evaluate the criteria for membership in the ALJLAP and to determine whether or not sufficient evidence exists to expand, limit or contract membership in the system in the future.

***TFTC recommendation:*** The TFTC concurs.

## *FINANCIAL SECURITY IN RETIREMENT*

### *HB 1847 – Formula increase legislation*

SRAC recommendation: This legislation would have increased the current benefit formula in the closed plans that are administered by MOSERS and HTEHPRS from 1.6% to 1.7% for all active, terminated-vested, and retired members. The SRAC opposes this formula increase in the closed plans. The SRAC recognized that the Year 2000 Plan was designed to specifically achieve certain policy and personnel objectives, correct benefit inequities, promote individual choice (current retirees may elect to transfer to the Year 2000 Plan), and to accomplish all of these goals without increasing the state's costs for retirement programs. Also, the SRAC believes that providing the 1.7% formula in the closed plan would be a step backward in the pursuit of benefit equity. The SRAC pointed out that the 1.7% formula is already available to all past, present, and future employees through the new plan and to incorporate that formula in the old plan would create a benefit disparity between the new and old plan.

*TFTC recommendation:* The TFTC concurs. While the benefit formula was increased in the Year 2000 Plan, certain features were eliminated as a cost reduction to offset the costs of the increased multiplier and the temporary benefit. Members of the closed plan retain these survivor and minimum COLA features. Increasing the multiplier while retaining these other features creates a significant benefit disparity between the Year 2000 plan and closed plans.

### *Retiree health care - Report of the House Interim Committee on Employee Health Care Contributions*

*SRAC recommendation:* The SRAC endorsed the desirable health care system characteristics noted by the House Interim Committee ***and proposed a structure which based the percentage of employer subsidy upon an employee's length of service.*** Given the current volatile nature of the health care industry, the SRAC believes a service-based health care model will serve as a future cost containment measure and will also ensure that the same quality of care is available to both the highest and lowest paid employees. The SRAC recommends adoption of the model that provides a subsidy towards a retiree's monthly premium of 2.5% per year of service based upon the applicable low cost plan option for each full year of actual state service with a maximum subsidy of 75%. The model does not include additional subsidies for dependent coverage. It should be noted, however, that the SRAC did not have unanimous support for this recommendation. In addition, after the SRAC completed its meetings the administration and the Missouri Consolidated Health Care Plan (MCHCP) took action to increase the health insurance subsidy for retirees for calendar year 2001.